Supreme Court, U. S.
FILED
AUG 12 1976
MICHAEL RODAK, JR., CLERK

APPENDIX

IN THE

Supreme Court of the United States

OCTOBER TERM, 1976

No. 75-1687

UNITED STATES TRUST COMPANY OF NEW YORK, as Trustee for The Port of Authority of New York and New Jersey Consolidated Bonds, Fortieth and Forty-First Series, on its own behalf and on behalf of all holders of Consolidated Bonds of The Port Authority of New York and New Jersey and all others similarly situated,

Appellant,

v.

THE STATE OF NEW JERSEY, BRENDAN T. BYRNE, Governor of The State of New Jersey, and WILLIAM F. HYLAND, Attorney General of the State of New Jersey,

Appellees.

APPEAL FROM THE SUPREME COURT OF NEW JERSEY

VOLUME II

Pages 529a—1149a

FILED MAY 21, 1976

PROBABLE JURISDICTION NOTED JUNE 28, 1976

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SUPERIOR COURT OF NEW JERSEY

LAW DIVISION—BERGEN COUNTY

STIPULATION

UNITED STATES TRUST COMPANY
OF NEW YORK, etc.
v.
THE STATE NEW JERSEY, et al.

The undersigned hereby stipulate, for the purposes of this action only, and subject to objections as to relevance, that the following statements are true and admissible into evidence.

I. THE PORT AUTHORITY OF NEW YORK AND NEW JERSEY

1. By virtue of Chapter 130 of the Laws of New Jersey of 1917 and Chapter 426 of the Laws of New York of 1917, the two States established study commissions to cooperate in making a thorough investigation of the conditions of the Port of New York, to submit a comprehensive report recommending the proper policy to be pursued for the best interest of the entire Port of New York, and to determine the legislation, State and Federal, necessary to make such recommendations effective "to the end that said Port shall be efficiently and constructively organized and furnished with modern methods of piers, rail and water freight, and adequately protected in the event of war."

2. The two State Commissions thereafter organized themselves into a single body known as the New York, New Jersey Port and Harbor Development Commission (the "Commission"). On December 16, 1920, the Commission issued a joint report summarizing its work, discussing Port conditions and setting forth a proposed compact and com-

Excerpts From Stipulation Among Counsel
Dated December 20, 1974

prehensive plan and maps and drawings depicting its findings and proposals. (Stip. 1) • • •

3. The 1920 Report outlined the chaotic, diverse, inadequate and congested Port facilities existing in 1920 restricting the flow of goods by railroad, steamship and motor truck in the Port area. Extensive discussions of the freight handling problems of carriers are contained in the 1920 Report. Except in passing, the 1920 Report did not deal with passenger transportation plans or facilities but rather the Report recommended proposed solutions to the problems involved in the movement of freight and commodities brought into, out of, and through the Port District. (Stip. 2) • • •

4. The 1920 Report recommended the adoption of a Compact between the two States, establishing a Port District and creating a Port Authority. It included an extensive discussion of the legal precedents concerning Congressional and State powers over interstate commerce. The Report stated:

> "Permissive or restrictive, as the case may be, the power of Congress over the instrumentalities of interstate traffic is exclusive, when in a specific case it has been exercised. But this latter limitation, coupled with the broad police power of the State and its control of intrastate commerce, has left to New York and New Jersey a broad field within which they may act without express Federal consent. It is hoped, of course, by securing congressional approval of any plan which may be adopted, to avoid future conflict with the Federal authority over interstate unification and control of the Port. But for the present the States may act alone." At p. 446.

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5. In response to the recommendations of the 1920 Commission and pursuant to the Laws of New Jersey of 1921, Chapter 151 and the Laws of New York of 1921, Chapter 154, commissioners of both States were appointed with authorization to enter into an agreement or compact in the form specified in the statute and to seek the consent of Congress in respect of the agreement. On April 30, 1921 the Compact between the two States (N.J.S.A. §§32:1-1 to 24; N.Y. Unconsol. Laws §§6401-6423) relating to the Port Authority of New York and New Jersey (the "Port Authority") was actually signed. Congressional consent to "each and every part and Article" of the Compact was obtained effective August 23, 1921. (Public Resolution No. 17. 67th Congress, First Session (42 Stat. 174)).

6. The Compact provided in part as follows:

The Preamble of the Compact states that "a better coordination of the terminal, transportation and other facilities of commerce in, about and through the port of New York, will result in great economies, benefiting the nation, as well as the states of New York and New Jersey" and that "the future development of such terminal, transportation and other facilities of commerce will require the expenditure of large sums of money, and the cordial cooperation of the states of New York and New Jersey in the encouragement of the investment of capital, and in the formulation and execution of the necessary physical plans." Article II of the Compact creates the Port of New York District comprising an area of about 1500 square miles in both states centering about New York harbor. Article III establishes the Port Authority as "a body corporate and politic, having the powers and jurisdiction hereinafter enumerated, and such other and additional powers as shall be conferred upon

it by the legislature of either state concurred in by the legislature of the other, or by act or acts of congress." Article IV states that the Port Authority shall consist of six Commissioners, three from each State.* The Commissioners were to be chosen "in the manner and for the terms fixed and determined from time to time by the legislature of each state respectively." Article VI of the Compact vests in the Port Authority "full power and authority to purchase, construct, lease and/or operate any terminal or transportation facility within" the Port District and authorizes the Port Authority "to borrow money and secure the same by bonds or by mortgages." Article VII provides that the Port Authority "shall have such additional powers and duties as may hereafter be delegated to or imposed upon it from time to time by the action of the legislature of either state concurred in by the legislature of the other" and further provides "the Port Authority shall not pledge the credit of either state except by and with the authority of the legislature thereof." Article XI requires the Port Authority to make plans for the development of the Port District supplementary to or amendatory of any plan theretofore adopted. Article XII authorizes the Port Authority to "make recommendations to the legislatures of the two states or to the congress of the United States, based upon study and analysis, for the better conduct of the commerce passing in and through the Port of New York." Article XV of the Compact provides that "Unless and until the revenues from operations conducted by the Port Authority are adequate to meet all expenditures, the legislatures of the two states shall appropriate, in equal amounts, annually for the salaries,

* By Chapter 244, Laws of New Jersey of 1930 and Chapter 419, Laws of New York of 1930 the number of Port Authority Commissioners was increased from six to twelve.

office and other administrative expenses, such sum or sums as shall be recommended by the Port Authority and approved by the governors of the two states, but each state obligates itself hereunder only to the extent of one hundred thousand dollars in any one year."* Article XXII defines "transportation facility" to include "railroads, steam or electric, motor truck or other street or highway vehicles, tunnels, bridges, boats, ferries, carfloats, lighters, tugs, floating elevators, barges, scows or harbor craft of any kind, aircraft suitable for harbor service, and every kind of transportation facility now in use or hereafter designed for use for the transportation or carriage of persons or property" and defines "railroad" as "including railways, extensions thereof, tunnels, subways, bridges, elevated structures, tracks, poles, wires, conduits, power houses, substations, lines for the transmission of power, car barns, shop yards, siding, turnouts, switches, stations and approaches thereto, cars and motive equipment."

7. By Laws of New Jersey of 19??, Chapter 9 and Laws of New York of 1922, Chapter 23, a Comprehensive Plan for the development of the Port of New York was adopted by the New Jersey and New York Legislatures. The Comprehensive Plan received the consent of Congress. Ch. 277, Public Res. No. 66, July 1, 1922, 42 Stat. 822. The Comprehensive Plan sets forth the development program initially envisioned for implementation by the Port Authority.

8. In the Comprehensive Plan of 1922, unification of terminal operations and facilities, consolidation of shipments, adaptation and coordination of existing facilities, im-

* The States paid the administrative expenses of the Port Authority through the year 1934. 1935 was the first year in which the Port Authority became self-supporting.

provement of commercial rail, truck and water facilities and other freight handling improvements are set forth as principles to govern the development of the Port Authority. The Comprehensive Plan proposed to establish direct freight connections between New Jersey and Manhattan to furnish "the most expeditious, economical and practical transportation of freight especially meat, produce, milk and other commodities comprising the daily needs of the people." (N.J.S.A. 32:1-29). Section 8 of the 1922 Comprehensive Plan statutes denies the Authority the power to levy taxes or assessments, and provides that the bonds or other securities issued by the Port Authority shall at all times be free from taxation by either State. (Stip. 4-9) • • •

11. The Progress Report of the Port Authority, 1923, made the following statements concerning congressional consent to the Compact and Comprehensive Plan:

> "Some of these powers were such as the States could grant without further action by Congress, but as carrying out many of the steps involved in the Comprehensive Plan by the Port Authority would necessarily involve matters of interstate commerce and the interstate carriers engaged therein, it was deemed of importance by the Commissioners that Congress—which has paramount power over interstate commerce—should give the sanction of Federal authority to the plan, and the Legislatures of both States, therefore, directed the Port Authority to apply to Congress for such power. . . .
>
> "It was only upon the consummation of this step [congressional consent] that the Port Authority became fully equipped to exercise the powers outlined in the compact and intended to be conferred by the two States.
>
> "The Comprehensive Plan is now legally authorized by the two States and the Congress of the United States and the police powers of the States and the interstate commerce power of the Congress are joined in effectuating the definite plan, with one coordinating body as the State and Federal instrumentality."

12. Pursuant to the Compact, Comprehensive Plan and subsequent amendments and supplements thereto, the Port Authority operates all of the interstate vehicular tunnels and bridges in the Port District (which include the Holland Tunnel, the Lincoln Tunnel, the George Washington Bridge, the Bayonne Bridge, the Goethals Bridge and the Outerbridge Crossing).

The Holland Tunnel had been constructed by separate State commissions pursuant to a compact between the States which received the consent of Congress. Chapters 49 and 50, Laws of New Jersey of 1918 and Chapters 70 and 178, Laws of New York of 1919, consented to by Congress, Chapter 11, Public Resolution No. 10, 66th Congress (S.409) (1919). In 1930 the Holland Tunnel was transferred to the Port Authority in order to enable it to honor its obligations to bondholders in the face of deficits incurred in connection with the Arthur Kill, George Washington and Bayonne Bridges and Inland Terminal No. 1. Chapter 247, Laws of New Jersey of 1930 and Chapter 421, Laws of New York of 1930.

Also pursuant to the 1921 Compact, the 1922 Comprehensive Plan and subsequent amendments and supplements thereto, the Port Authority owns and/or operates the fol-

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lowing facilities: Newark International Airport, Teterboro Airport, La Guardia Airport, John F. Kennedy International Airport, two heliports; Port Newark, the Hoboken Port Authority Marine Terminal, the Elizabeth Port Authority Marine Terminal, the Columbia Street Marine Terminal, the Erie Basin Port Authority Marine Terminal and a Mid-Manhattan Consolidated Passenger Ship Terminal; the Port Authority Bus Terminal, the George Washington Bridge Bus Station, the Newark and New York Union Motor Truck Terminals; the Port Authority Trans-Hudson System (operated for the Port Authority through its wholly owned subsidiary, the Port Authority Trans-Hudson Corporation) and the World Trade Center. (Stip. 10-12)

• • •

II. NEW JERSEY'S PUBLIC TRANSPORTATION REQUIREMENTS.

A. Demographic and Transportation Factors.

• • •

3. The following is an excerpt from the 1972 Master Plan of the New Jersey Department of Transportation:

"New Jersey is now the most densely populated State in the Nation. Its problems of urbanization will continue to mount along with its growth in population, industry, commerce and recreational facilities and with the State's increasing importance as the geographic center of the Northeast 'megalopolis.'

"In the past, this growth has meant:

"The highway system has been unable to keep pace with travel demand. The density per lane-mile of daily travel has increased by 56.7 percent over the past 20 years.

"Paradoxically, coincident with a signficant decline in suburban passenger rail service, there

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has been, in recent years, an increased public demand for improved commuter rail service. At present, during the morning peak hour over 54,000 people make the trip between New Jersey and Manhattan by rail.

"Bus service has shown a continual decline in the last decade, yet in the morning peak hour more than 55,000 persons travel by bus from New Jersey to Manhattan.

"A 32 percent increase* in population through 1990 will result in the changing of more than 1,300 square miles of land from rural use to urban use.

"By 1990, motor vehicle registrations in the State will rise to 5,384,000—up 42 percent.

"Annual vehicle miles of travel on the State Highway System will increase 109 percent through 1990, registering a total of 28.1 billion vehicle miles.

"As a result of increased personal income and leisure time there will be a significant increase in recreation-oriented travel on the State's highways.

"Passenger rail patronage will experience a 75 percent increase to total 626 thousand daily riders in 1990.

"Bus ridership will increase to 1.6 million daily riders by 1990, an increase of 24 percent.

"A comprehensive plan to meet the 20-year needs resulting from this growth in the future is estimated to cost almost $7.0 billion. It includes:

*The latest official projection of the State of New Jersey is for a 27 percent increase during the same period (Population Estimates for New Jersey, July 1, 1973, p. 16) [footnote added by stipulation].

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"The highway plan will total $4.276 billion including $900.0 million for completion of the Interstate System, $1.866 billion for the construction of other freeways, $734 million to dualize presently undivided facilities, $588.0 million for widenings and $188 million to correct troublesome spot locations.

"On the State's passenger rail system, including commuter rail and rapid transit, the costs will amount to $1.897 billion.

"An additional $278 million is the estimated cost to provide bus riders of the State with adequate, modern service.

"The above breakdown of estimated costs does not include the anticipated escalation in costs over the 20-year time frame of the plan.

"PASSENGER RAIL SERVICES

"The commuter railroad system is operated by five companies which provide service to an average of 166,130 weekday passengers on a total of 467 route miles.

"Rapid transit services are provided by two public agencies* and one public company** on a total of 26 route miles providing service to an average of 192,400 weekday passengers.

"The total network of passenger rail systems provide service to 15 of the State's 21 counties, the ex-

*Port Authority operates PATH and the Delaware River Port Authority operates PATCO. [footnote added by stipulation]

**Transport of New Jersey operates the Newark subway. [footnote added by stipulation]

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ceptions being Burlington, Cumberland, Gloucester, Salem, Sussex and Warren Counties.*

"In 1950, there were approximately 1,100 route-miles of track in existence in the State providing commuter service to 20 counties, and there were more than 349,000 passenger trips a day. The decline in service over the past 20 years has resulted in only 467 route-miles of track remaining in use today, providing service to 15 counties with only 166,000 passenger trips daily.

"However, existing rapid transit facilities provide service for an additional 192,000 passengers per day. Total rail utilization now averages 358,000 passenger trips per day.

"Although there has been a significant decline in annual rail trips between New Jersey and New York, rail patronage during the commuter peak periods has remained constant.

"While still providing service, the Penn Central, Reading and Lehigh Valley Railroads have gone into bankruptcy in recent months. The Central Railroad of New Jersey has been in bankruptcy since 1967. (Stip. 17-20)

• • •

"THE CORRIDOR STATE

"While the above indicators can be related to growth within the State's boundaries, New Jersey also is in the unusual position of experiencing considerable travel across her boundaries. Because of this, New Jersey has been aptly termed the 'Corridor State.'

*Subsequent to the 1972 Report rail passenger service has been renewed to Warren County. [footnote added by stipulation]

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"This considerable interstate movement is attributable in part to New Jersey's location in the geographic center of megalopolis. The influence of the great urban centers of New York City and Philadelphia has caused the number of people crossing between New Jersey and Pennsylvania to be ranked highest in the Nation while the movements between New Jersey and New York is second highest.

"The largest single movement—commuter travel between New Jersey and Manhattan—amounts to 480,000 person-trips daily. Of this number, slightly less than 50 percent use some form of public transit —rail or bus. The morning and evening peak-hour movements are especially significant. During one peak hour in the morning more than 123,000 commuters cross the Hudson River into Manhattan. Of this total, 87 percent use some form of public transit.

"While the commuter problem is not as severe between the Camden area and Philadelphia, the same trend has emerged. One result has been the construction of the Lindenwold High Speed Line aimed principally at meeting the demand for interstate commuter travel.

"With the expectation that many of New Jersey's rural areas will become suburban 'bedroom communities' for highly concentrated urbanized areas, it is expected that the density of travel across the State's borders will become even more significant in the future. (Stip. 20-21)

• • •

"Before a plan can be developed outlining a solution to serve the transportation needs of the State, a set of objectives—specific goals toward which effort is directed—must be derived. Such a listing of

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objectives can lead to policy guidelines defining the atmosphere in which transportation needs can be met.

"TRANSPORTATION OBJECTIVES

"Provide a transportation network equitable to all segments of the State populace

"Increase comfort and convenience of travel

"Reduce adverse impacts on the natural environment

"Promote desired pattern of land development

"Increase safety

"Reduce travel time and cost per trip

"Provide a choice of travel modes

"Be realistic in terms of physical, social, financial and environmental restraints

"POLICY GUIDELINES

• • •

"COMMON CARRIER

"Maintain and strengthen the existing rail and bus system by replacing obsolete equipment.

"Improve the efficiency and quality of rail and bus operations.

"Extend service to areas deficient in service.

"Improve coordination within the total transportation system. (Stip. 22)

• • •

"CORE SECTOR

"The core sector includes all of Hudson County, Newark, and the adjacent portions of the municipalities surrounding Newark. Travel in this sector has several distinct patterns. The Newark portion is

heavily oriented to the Newark Central Business District, with a relatively low level of travel to Manhattan. The Hudson County portion of the sector has a large amount of local, relatively short distance, travel. Trips to Manhattan are most prevalent from the area north of the Lincoln Tunnel. Most travel in the core sector is by bus. The only major rail movements are on PATH, between southern Hudson County and Manhattan, and on the Newark subway. Rail improvements in this sector will be designed to improve travel to and within the Newark CBD and to solve the specialized problem of access to Newark Airport.

"NEWARK AIRPORT ACCESS—Rail access to Newark Airport will be designed to provide service to a variety of points including Manhattan and the Newark central business district.

"This access would be provided by an extension of the tracks of the Port Authority Trans-Hudson Corporation—(PATH) from the present terminus in Penn Station—Newark. A transfer station will be located on airport property west of the Newark Airport terminal complex. This station will permit passengers to transfer to and from the proposed Inter-Terminal Transportation System (ITTS) which will inter-connect the three terminal buildings of the new complex.

"The rail access proposal will connect with and use tracks on the Central Railroad of New Jersey right-of-way near Elizabethport Yard and will continue westward to a terminus that must be determined. A park-ride facility near the crossing of the CNJ main line and the Garden State Parkway is one possible

terminus. Extension of the service to either Plainfield or to the Raritan area is also being considered.

"CENTRAL SECTOR

"The Central Sector includes the area of the State extending from New Jersey Route 3 and U.S. Route 46 on the north to and including the New Jersey Turnpike between Perth Amboy and Bordentown on the South. Suburban rail service is provided in three major corridors by the Morris and Essex Line of the Erie Lackawanna, including the Gladstone Branch; the Main Line of the Jersey Central and the Main Line of the Penn Central. Additional suburban service is provided on the Greenwood Lake and Montclair Branches of the Erie Lackawanna and the New York Branch of the Reading. Travel in this area is largely oriented to Manhattan with a secondary focus at Newark. The majority of commuter travel to Manhattan is by rail, with some bus travel to midtown Manhattan. Most travel to Newark is by bus, with rail travel important only for the longer distances.

"Rail service in the central sector is oriented to three Manhattan entry points. These points of entry are the Penn Central tunnel and the Midtown and Downtown PATH tunnels serving the 33rd Street and World Trade Center areas respectively. Access to Newark is at two points; the Erie Lackawanna and Penn Stations. With the exception of the Morris and Essex, all lines have access to all Manhattan entries. The only direct service provided to Penn Station, Manhattan, is from the Penn Central Main Line. Access from other lines to Penn Station, New York, as well as all access to Manhattan via

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Dated December 20, 1974

PATH, requires a transfer. One of the principal goals of planning for this sector is to improve Manhattan access, including access to Penn Station, New York, for all lines and direct service to some point on Manhattan for all lines. (Stip. 24-25)

• • •

"Financial Considerations

"The ability of the Department to successfully implement this Master Plan over the next 20 years is tied inextricably to the annual funding of its construction programs.

"The financing of highways, under existing federal programs, is fundamentally different from the programs for the other modes in that it is based on annual apportionments to the various states based on a pre-set formula—whereas UMTA [Federal Urban Mass Transportation Administration] and FAA furnish federal capital funds on a grant basis for each proposed project for which an acceptable application has been filed.

"Fiscal projections based on historic data assure that normal transportation funding will have to be augmented by substantial amounts of additional monies annually.

"As stated earlier in the report all indicated costs are based on present day estimates and have not been escalated to reflect inflationary costs. No attempt has been made to establish priorities during the development of the Master Plan. Consequently, the individual projects have not been scheduled or programmed. It would therefore, not be realistic to attempt to expand the cost of the individual components without precise knowledge as to the year of contract award.

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"On the other hand, it would be fair to assume that the economic history of this country proves there will be an increase in these costs over the next 20 years.

"Funding Gap to Implement 20 Year Plan

Highway Construction	$4276.0	
Federal and State Matching Programs	2332.0	
Deficiency		–$1944.0
Railroad Passenger Service	$1897.0	
Federal UMTA Grants	1264.7	
Local Matched Share (State)		–$ 632.3
Bus Service	$ 278.0	
Federal UMTA Grants	185.3	
Local Matched Share (State)		–$ 92.7
Airport Development Program	$ 49.0	
Federal Aviation Administration Grants	24.5	
Local Matched Share (State)		–$ 24.5
Total Funding Gap		$2693.5

(All Amounts in Millions)". (Stip. 27-28)

• • •

6. The four private companies which operate commuter railroad services in New Jersey are all being reorganized under federal bankruptcy laws. Three of these four companies reported operating at a deficit in 1960; they attributed their deficits to losses incurred on passenger rail mass transit operations even though one had lower passenger losses than when it operated at a profit and another's deficit was twice as large as its passenger loss. (Farley Committee Hearings, January 26, 1961, pp. 17-22). The four railroads reported to Highway Commissioner Palmer the following results for 1959 and 1960:

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	1959 passenger deficit	1959 corporate profit or deficit	First 11 months of 1960 corporate profit or deficit	Estimated 1960 passenger deficit
Pennsylvania	($37,000,000)	$ 7,200,000	($ 5,000,000)	($32,000,000)
Erie Lackawanna	($ 8,000,000)	($10,000,000)	($16,000,000)	($ 8,100,000)
Reading	($ 7,000,000)	$ 1,800,000	$ 1,100,000	($ 7,000,000)
Central	($ 6,300,000)	($ 2,800,000)	($ 3,400,000)	($ 6,000,000)

7. Reorganization proceedings for the Central Railroad Company of New Jersey were instituted in 1967, for the Penn Central Transportation Company and for the Reading Company in 1970 and for the Erie Lackawanna Railway in 1972. (1973 Program, page 17). The 1973 [New Jersey Department of Transportation Transit Development] Program (Exhibit I) published on September 1, 1973, said of these proceedings:

> "In several cases, the Federal District Courts have instructed the railroad companies to prepare plans for the cessation of passenger and freight service, and in these cases, it is the policy of the State of New Jersey to impress upon the federal courts the necessity of continuing most of these rail services." (1973 Program, page 17).
>
> "Cessation of mass transportation services in these urban areas [refers to the Philadelphia as well as the New York City area] would produce intolerable conditions on the personal lives of the residents of the areas. The State is now directed by the federal government to reduce the levels of air pollution in these areas to a significant degree within the next five years. It has been determined that the existing basic rail and bus systems will fail within the next few years unless a major investment in capital facilities, equipment, and operating subsidies is provided by the public." (1973 Program, page 19).

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8. On January 2, 1974, Congress enacted the regional Rail Reorganization Act of 1973 (45 U.S.C. §701 *et seq.*). Congress found and declared in this statute that: "Essential rail service" in the midwest and northeast region is provided by railroads that are insolvent and attempting to undergo reorganization under the Bankruptcy Act; "this essential rail service is threatened with cessation or significant curtailment because of the inability of the trustees of such railroads to formulate acceptable plans of reorganization"; the public convenience and necessity require adequate and efficient rail service in this region "to meet the needs of commerce, the national defense, the environment and the service requirements of passengers, United States mail, shippers, States and their political subdivisions, and consumers"; "continuation and improvement of essential rail service in this region is also necessary to preserve and maintain adequate national rail services and an efficient national rail transportaion system"; "rail service and rail transportation offer economic and environmental advantages with respect to land use, air pollution, noise levels, energy efficiency and conservation, resource allocation, safety, and cost per ton-mile of movement to such extent that the preservation and maintenance of adequate and efficient rail service is in the national interest"; and that these needs could not be met without substantial federal participation. Among the goals of the federal plan for reorganization and modernization of the railroads in the northeast corridor are: the establishment of improved high-speed rail passenger service; the utilization of those modes of

transportation in the region which require the smallest amount of scarce energy resources and which can most efficiently transport energy resources; the attainment and maintenance of any environmental standards, particularly the applicable national ambient air quality standards and plans established under the Clean Air Act Amendments of 1970; and the movement of passengers and freight in rail transportation in the most efficient manner consistent with safe operation, including the requirements of commuter and intercity rail passenger service.

The Act established the United States Railway Association, which was authorized to carry out the purposes of the Act and in furtherance thereof to issue bonds, debentures, securities or other obligations guaranteed by the Secretary of Transportation, with the maximum aggregate amount of obligations outstanding at any one time not to exceed $1.5 billion. Pending implementation of the final system plan, the Secretary of Transportation was authorized to expend up to $85 million to be paid to the trustees of railroads in reorganization for the continued provision of essential transportation services by such railroads.

With respect to local rail service, Congress found and declared (45 U.S.C. § 762) that: "The Nation is facing an energy shortage of acute proportions in the next decade"; "railroads are one of the most energy-efficient modes of transportation for the movement of passengers and freight and cause the least amount of pollution"; "abandonment, termination, or substantial reduction of rail service in any locality will adversely affect the Nation's long-term and immediate goals with respect to energy conservation and environmental protection." Accordingly, the Secretary was directed to provide financial assistance to States or local or

regional transportation authorities for the purpose of rail service continuation subsidies, 70% of which is to be paid by the federal government and 30% of which is to be paid by the affected State. Federal funding up to $90 million total per year for 2 years is authorized. The Secretary was authorized to issue regulations within 90 days to put this program into effect. Such regulations have not yet been promulgated. On December 16, 1974 the Supreme Court of the United States upheld the constitutionality of the Act.

9. Pursuant to the Regional Rail Reorganization Act of 1973 the United States Railway Association has submitted a plan recommending that approximately 300 miles of trackage owned by bankrupt railroads in New Jersey be abandoned. (Stip. 30-35) • • •

In October 1974, Alan Sagner, the New Jersey Commissioner of Transportation publicly stated that even if the final federal plan called for a reduction of 150 miles of rail lines in New Jersey, "that could have a disastrous impact on our economy and environment." At the request of Governor Byrne, the New Jersey Legislature approved for submission to the voters of New Jersey in the November, 1974 elections a proposed $100 million rail preservation bond issue that would allow the State to purchase railroad rights-of-way that would be abandoned under the federal plan. This bond issue was defeated in the November, 1974 election by a vote of 893,622 to 854,083.

10. In September, 1974 Commissioner Sagner stated publicly:

(1) The State of New Jersey has not yet spent $106 million of the mass transportation bond issue of $200 million authorized in 1968. The bulk of this money is expected to be obligated within the next year on the reelectrification of

and the purchase of 200 new commuter cars for the Morris & Essex Division of the Erie-Lackawanna Railroad, electrification of the New York and Long Branch Railroad from South Amboy to Red Bank and the purchase of 1,500 new buses and 300 used buses, but $68 million of the total funds is expected to remain contractually uncommitted as of July 1, 1975.

(2) According to 1970 census figures 3.6% of the 2,839,545 people in New Jersey who work commute by railroad.

11. In support of a $200 million proposed bond issue for highways, Commissioner Sagner said in his question and answer release of September, 1974:

> "1. We should not ask for new money for public transporation projects until we have met the following criteria:
>
> "We have obligated the money the voters authorized in 1968; we hope to do this within a year. We developed a *comprehensive* public transportation plan that will show the voters what type of public transportation service will be available after the expenditure of necessarily large sums of capital. This study is underway, but will take at least a year to complete. We should also, at that time, be able to predict the annual operating subsidy needed to maintain the public transportation system. The voters should be prepared to undertake this obligation when they approve a project."

"2. Improving the roads without providing a mass transit alternative will encourage a greater use of cars and will add to the problem of air pollution when we are trying to reduce it. Isn't that correct?

"The Department is developing public transportation programs, but no matter what is done, individual cars will be used for the foreseeable future. The New Jersey Energy Office and the Tri-State Regional Planning Commission have publicized statements indicating that congestion, as opposed to free-moving traffic, increases pollution.

"3. Some groups say the highway safety and improvement bond issue would do nothing for mass transit. Is that true?

"The most vital and widespread form of mass transit now and in the foreseeable future is the bus. The bus travels on highways.

"4. If the highway projects are so important, why aren't you willing to make this a combined highway-public transit bond issue, if only to get the support of the public transit advocates, and thereby give the highway portion a better chance of approval?

"As explained, it would be irresponsible to request funds *now*, for a public transportation bond issue as the public transportation money is not needed *now*. Proposing a combined highway safety and improvement public transit bond issue to win support of the public transit advocates and environmentalists would not be honest. A serious problem in government today is the inability of the citizens to trust public officials. In the long run such tactics would result in the Department losing credibility and support for all future efforts." (Stip. 36-39) • • •

B. The Energy Crisis

1. On February 4, 1974, the New Jersey Legislature enacted the Emergency Energy Fair Practices Act of

1974 (L. 1974, c. 2, amended and supplemented by L. 1974, c. 6). Section 2 of this Act stated: "The Legislature finds and determines that because of world conditions and the manner in which energy sources and fuels are allocated and distributed that an energy shortage now exists and may continue for the foreseeable future." Section 3 of the Act authorized the Governor "to proclaim by Executive Order the existence of an energy emergency" and to establish a State Energy Office and appoint an Administrator with broad powers to control the use and distribution of all fuels.

2. On February 5, 1974, Governor Byrne issued Executive Order No. 1 in which he proclaimed the existence of an energy emergency, created the State Energy Office and established the position of Administrator of that Office.

3. On or about March 14, 1974, a civil action entitled *Byrne, et al.* v. *Simon, et al.,* Civ. No. 74-372, was instituted in the United States District Court for the District of New Jersey in which the complaint alleged that the State of New Jersey had not received from the Federal Energy Office an equitable allocation of gasoline for the month of March 1974.

4. In support of an application for an Order to Show Cause, plaintiffs in *Byrne* v. *Simon* submitted an affidavit dated March 13, 1974 by Richard W. DeKorte, who had been appointed Administrator of the New Jersey Energy Office. Paragraph 4 of that affidavit stated:

> "In many communities there were wholesale closings of service stations. As a result, large numbers of people were totally unable to obtain gasoline and therefore were prevented from either engaging in

> their respective employments or from obtaining necessary food supplies, medical services, and other necessities of life. An already high unemployment rate was threatened with further increases. This was due to the fact that many employers were not able to obtain deliveries of necessary products and were faced with situations where many employees were either tardy or not coming in at all. Obviously, there were severe economic dislocations in the business community.
>
> "In those areas where a few retail gasoline stations were in fact open, it was commonplace to observe long lines of cars extending on to the public roads of New Jersey that were waiting for gasoline. Ingress and egress to homes and commercial establishments on many occasions were blocked. Traffic on said roads were severely disrupted. The threat of serious accidents not only to property but more importantly to life was constantly present. And tensions and emotions were rising to dangerously high levels. State and local law enforcement personnel were on alert in order to be prepared for public safety problems of the worst magnitude.
>
> "Emergency services were severely cut back. It was not uncommon to learn of local law enforcement personnel, first aid personnel, and fire fighting personnel that were not able to obtain sufficient quantities of motor gasoline that allowed them to be anywhere near the minimum state of readiness that is necessary for them to carry out their responsibilities."

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There is no shortage of gasoline in the State of New Jersey as of December, 1974.

5. In a news release issued on December 3, 1973 the Regional Plan Association commented on the relationship of the energy crisis to transportation [in the tri-state New York urban region]: (Stip. 43-45) • • •

"ENERGY FOR TRANSPORTATION

"Fuel for transportation has shown the second largest absolute growth, following that for electricity generation.

Passenger

"Passenger transportation consumption rose from 367 trillion Btu of gross input in 1950 to 904 trillion Btu in 1970. This increase is attributable to five factors:

"1. *Population growth* accounts for 32 percent of the increased consumption.

"2. *More autos per capita and longer trips* (mostly by air) resulted in more miles of travel per person, which explains 26 percent of the increase in fuel use. The frequency with which people make trips increased somewhat, mostly due to wider automobile ownership. The length of the average trip increased considerably mostly due to more trips to and from points outside the Region.

"3. *The shift away from buses and rail* vehicles toward more energy intensive modes, such as autos, and airplanes, accounts for 20 percent of the increase.

"4. *Declining vehicle occupancy*—fewer persons per car, per bus or rail car, accounts for 12 percent.

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"5. *The increasing energy-intensity of each mode of travel*—more gasoline needed per mile—because of higher performance, more air conditioning, etc. explains 10 percent.

Energy Use of Modes of Travel

"*Bus* is the least energy-intensive mode, requiring about 2,300 Btu per passenger mile of travel.

"*Rail,* combining both electric and diesel-electric traction, uses 2,600 Btu of Gross input per passenger mile but carries passengers more than three times faster than a bus in return for the 15 percent higher use of energy per passenger.

"*Subways,* with 3,100 Btu per passenger mile, are more energy-intensive because of the stop-and-go operation, which wastes much energy in braking. New devices to eliminate some of this waste are being tested by the Metropolitan Transportation Authority.

"*Auto,* using 6,500 Btu per passenger mile in 1970, was twice as intensive as the subway.

"*Air,* using 11,600 Btu per passenger mile, uses twice as much energy as the auto.

"*Taxi-cabs and private airplanes* (general aviation) are most energy-intensive." (Stip. 48-49) • • •

6. The United States consumes 18 million barrels of petroleum a day, but produces only 11 million of those barrels from domestic sources. The difference is made up by imports. Presidental Message to Congress on the En-

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ergy Crisis, U.S. Code. Cong. and Admin. News, 93rd Cong., 2d Sess. at 31, 32 (Feb. 21, 1974, monthly ed.)

7. President Nixon went on to say:

> "We must also face the fact that when and if the oil embargo ends, the United States will be faced with a different but no less difficult problem. Foreign oil prices have risen dramatically in recent months. If we were to increase our purchase of foreign oil, there would be a chronic balance of payments outflow which, over time, would create a severe problem in international monetary relations." *ibid* at 36.

8. President Nixon also noted that the United States would "continue to be vulnerable to interruptions of foreign imports." *ibid.*

9. President Nixon further noted that Project Independence had been put forward to phase out dependence upon high priced foreign oil, with its attendant risk of economic breakdown at the will of oil producers. Project Independence entails three concurrent tasks: expansion of domestic energy supplies; conservation; and new energy research. On conservation, the President wrote, "We must reduce demand by eliminating non essential energy use and improving the efficiency of energy utilization." *ibid.* President Nixon stated: "It is now widely recognized that the development of better mass transit systems may be one of the key solutions to both our energy and environmental problems." *ibid* at 42. (Stip. 50-51) • • •

12. According to figures compiled from Survey of Current Business, and BP Statistical Review, automotive gasoline comprises roughly 40% of the total demand for oil.

Excerpts From Stipulation Among Counsel
Dated December 20, 1974

C. Health and Environmental Factors

1. In 1950, pursuant to a resolution of the Senate and General Assembly, a legislative commission was created to study air pollution in New Jersey and to recommend legislation. (House Concurrent Resolution No. 16; Senate Concurrent Resolution No. 9, 1951)

2. The commission referred to in the immediately preceding paragraph issued a report to the New Jersey State Legislature in March, 1952 which included a review of air pollution conditions and legislation in other states and recommendations for air pollution abatement legislation in New Jersey. The 1952 report pointed out that air pollution was caused by a variety of activities and that industry alone was not responsible for it (Report, p. 28). The 1952 report specifically noted that emissions from automobiles contributed to air pollution. (See, for example, Report pp. 38, 67)

3. New Jersey enacted in 1953 The Smoke Control Code of New Jersey, N.J. Rev. Stat. 26:3-69.6, which prohibits emission of smoke of a certain density. The Smoke Control Code of New Jersey was subject to adoption by reference by local Boards of Health and was not enforceable until adopted.

4. The New Jersey Bureau of Adult and Occupational Health instituted in 1953 a comprehensive air sanitation program. The three objectives of that program were to assist in the establishment of local control of air pollution, to conduct air sanitation research, and to provide technical and scientific assistance in solving the problem of excessive air pollution.

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5. In 1954, the New Jersey Air Pollution Control Act was enacted into law (Chapter 212, Laws of New Jersey of 1954). Under its provisions, an Air Pollution Control Commission was appointed by the Governor as an agency of the State Department of Health. The Commission was empowered to promulgate and amend codes to control and prohibit air pollution in the State . The State Department of Health had the responsibility of controlling air pollution in accordance with any code, rule or regulation promulgated by the Commission.

6. President Dwight Eisenhower in 1955 noted in his special health message:

> "As a result of industrial growth and industrial development, the atmosphere over some population centers may be approaching the limit of its ability to absorb air pollutants with safety to health."

Congress enacted in the same year the Air Pollution Control—Research and Technical Assistance Act which authorized the Department of Health, Education and Welfare, through the United States Public Health Service, to utilize the resources of the Federal Government and to cooperate with State and local governments and educational institutions in the preparation and execution of programs of research into the problem of air pollution. Senate Report No. 389, May 27, 1955 stated that one of the reasons for the legislation was the serious nature of the air pollution problem. (Senate Report pp. 2457, 2559)

7. A study was conducted in the summer and fall of 1957 by the Interstate Sanitation Commission of smoke and air pollution in certain areas of New York and New Jersey.

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The study found, among other things, that, although there were many sources of air pollution in Newark, the primary source at the point sampled was traffic gases. The primary source of air pollution in Manhattan was also found to be motor vehicle traffic.

> "A study of air pollution by the Interstate Sanitation Commission in 1957 confirmed that there is considerable transport of air contaminants across the New York and New Jersey state boundaries in both directions, depending on wind and weather conditions.
>
> "The prevailing wind direction is north-westerly. This means that even if the New York City Department of Air Pollution Control were to attain 100 per cent effectiveness in its work against local sources of air pollution, New York City would still have an air pollution problem of substantial magnitude, and one which will continue to grow." (Stip. 52-56) • • •

8. In the 1950's New York State conducted several statewide surveys to assess New York's air pollution problem. One of these studies begun in 1952 by the Joint Legislative Committee on Pollution Control culminated in the passage of the Air Pollution Control Act in 1957 (Article 12-A, Chapter 931, Laws of New York). This Act amended the Public Health Law and was designed to safeguard the State's air resources by (a) detecting, controlling or abating existing air pollution and (b) preventing new air pollution. Administration of the act was delegated to the Air Pollution Control Board which was created within the New York State Department of Health. The Board has

the power to adopt and enforce rules and regulations for prevention and control of air pollution. Other important board functions include provision of advisory technical consultation services; development and conduct of demonstration programs in cooperation with communities; training local personnel, and supervision of air pollution control education.

9. In March 1960, the City Administrator of the City of New York issued a report entitled "Air Pollution Control: Organization and Operation." This report stated:

> "We find . . . there is little evidence of any absolute decline in the amount of air pollution as a result of the department's activities. The best that can be said is that the volume of pollutants would probably have been greater if there had been no control program . . ."

* * *

15. The United States Clean Air Act, as amended in 1970, requires the Administrator of the Environmental Protection Agency to establish national primary and secondary air quality standards for air pollutants. 42 U.S.C. §1857C-4. Primary ambient air standards shall be such as "are requisite to protect the public health." 42 U.S.C. §1857C-4(b)(1). Secondary ambient air quality standards "shall specify a level of air quality the attainment and maintenance of which . . . is requisite to protect the public welfare from any known or anticipated adverse effects associated with the presence of such air pollutant in the ambient air." 42 U.S.C. §1857-4(b)(2).

16. Pursuant to Section 107(b) of the Clean Air Act, 42 U.S.C. §§1857-1857(1), the Commissioner of the National Air Pollution Administration has been delegated authority

to issue air quality criteria reports to facilitate formulation of standards on the basis of up-to-date scientific knowledge concerning the full range of effects of pollutants. The National Air Pollution Control Administration issued its reports, Air Quality Criteria For Carbon Monoxide, Publication No. AP-62 (1970) and Air Quality Criteria for Hydrocarbons, Publication No. AP-64 (1970) pursuant to that authority. The current levels of these pollutants in the air of the New Jersey-New York-Connecticut metropolitan region are in excess of federally-mandated standards.

17. Air Quality Criteria for Carbon Monoxide, National Air Pollution Control Administration Pub. No. AP-62 (1970), stated that "the largest single source of CO (carbon monoxide) is the exhaust of motor vehicles, both gasoline and diesel powered." (AP-62 page 4-2). In the New York Metropolitan area, an estimated 95.5% of all CO emissions came from transportation. (*Ibid.* page 4-6). Air Quality Criteria for Hydrocarbons, National Air Pollution Control Administration Publication No. AP-64 (1970), stated that, on average, 70 percent of hydrocarbon emitted into the air came from transportation sources. (AP-64 page 2-14). (Stip. 58-60) * * *

20. The Federal report on carbon monoxide found that low concentrations of COHb [carboxyhemoglobin] in the blood of experimental subjects produced impairment in time-interval discrimination, changes in visual acuity and relative brightness threshold, and an impairment in capacity to perform psychomotor tests. (AP-62 at pages 8-51, 8-52).

21. The Federal report on carbon monoxide found that the following cardiovascular changes have been observed at COHb levels above 5%:

"Increased cardiac output, systemic arterio-venous oxygen-content differences, systemic oxygen extraction ratios, myocardial arterio-venous oxygen-content difference, and coronary blood flow in patients without coronary heart disease." (AP-62 at page 8-52).

22. The Federal report on carbon monoxide noted that

"the population group most susceptible to the adverse effects of atmospheric CO can be predicted on a physiological basis to include those persons most sensitive to a decrease in oxygen supply: (1) people with severe anemia due to the already limited supply of oxygen-carrying hemoglobin; (2) those with cardiovascular disease and the resultant impairment of circulation; (3) those with abnormal metabolic states such as thyrotoxicosis or fever, which result in increased oxygen demands; (4) those with chronic pulmonary disease; and (5) the developing foetus." (AP-62 at page 9-8).

23. The Administrator established national primary and secondary ambient air standards for carbon monoxide which he judged necessary to "protect the public health." 40 CFR § 50.2. The standards call for concentrations no greater than 10 mg. per cubic meter (9 parts per million) at a maximum eight hour concentration not to be exceeded more than once a year, and 40 mg. per cubic meter (35 parts per million) at a maximum one hour concentration not to be exceeded more than once a year. 40 CFR § 50.8.

24. The Federal report on carbon monoxide noted:

"No long-term human studies on experimental CO exposures have been reported, although there are

data on occupational exposures. Brief exposures to high levels of CO have produced effects on the central nervous, vascular, and respiratory systems." (AP-62 at pages 8-46)

"In many of the human studies, the brief exposures to very high levels of CO make it difficult to relate the observed effects to equilibrium COHb levels. For long-term exposure to CO, certain effects such as increased hematocritis, hemoglobin levels, and blood volume may be present, but the available data are inadequate to draw firm conclusions concerning the significance of all of these changes." (AP-62 at pages 8-51)

"Long-term experimental exposure of humans to CO may produce certain adaptive effects such as increased hemoglobin levels and hematocritis, but the available data are inadequate to draw firm conclusions. Such effects have been observed in animals. There is a definite need to further evaluate the effect of cigarette smoking on the central nervous system and cardiovascular system, as well as the possible 'adaption' of the cigarette smoker to CO." (AP-62 at pages 8-52)

"Research on the physiology of CO in the human body has provided considerable information on both endogenous CO production and on the effects of CO at various cellular and microcellular levels. Our knowledge of the effects of CO on enzyme systems and tissue oxygenation, however, is far from complete. In addition, mechanisms of CO catabolism in the body remains undefined. The uptake of CO dur-

ing varying time periods and with changes in activity must be further demonstrated.

"Studies of the effects of CO on human behavior and performance need both clarification and replication. Definition and sophistication of parameters sensitive to changes in blood hemoglobin merit considerable attention as a prerequisite to better defining the influence of CO on human performance." (AP-62 at page 10-5)

25. The federal report on hydrocarbons, National Air Pollution Control Administration Publication No. AP-64, covers "the class of hydrocarbons . . . which exist in the atmosphere in the gas phase." The report notes that "[m]any of these compounds may enter into atmospheric photochemical reaction processes leading to the products and manifestations associated with photochemical air pollution." (AP-64 at page 2-1). Motor vehicles are responsible for 49 percent of hydrocarbon emissions. (AP-64 at page 2-12).

26. The hydrocarbon report notes that "health effects (including eye irritation), vegetation damage, material damage, and visibility reducton have all been associated with the products that result from the interaction of hydrocarbons within the nitrogen dioxide atmospheric photolytic cycle." (AP-64 at page 5-1). (Stip. 61-64) •••

28. The Administrator of the Environmental Protection Agency set national primary and secondary ambient air quality standards for hydrocarbons which he judged necessary to "protect the public health". 40 CFR § 50.2 et seq. These standards call for maximum concentrations of 160 mg. per cubic meter (0.24 ppm) for a three hour concentration (6-9 A.M.) not to be exceeded more than once a year. 40 CFR § 50.10. Implementation of this standard is necessary to achieve the national standards for photochemical oxidants, which are produced by reactions with hydrocarbons. The national primary and secondary air quality standards for photochemical oxidants call for concentrations of 160 mg. per cubic meter (0.08 ppm) maximum one hour concentration, not to be exceeded more than once per year. 40 CFR § 50.9. (Stip. 65)• • •

The [hydrocarbon] report concluded that:

> "Our present state of knowledge does not demonstrate any direct health effects of the gaseous hydrocarbons in the ambient air on populations, although many of the effects attributed to photochemical smog are indirectly related to ambient levels of these hydrocarbons." (AP-64 at page 8-4&5)
>
> ". . . it has been demonstrated that ambient levels of photochemical oxidants which do have adverse effects on health, are a direct function of gaseous hydrocarbon concentrations; and when promulgating air quality standards for hydrocarbons, their contribution to the formation of oxidants should be taken into account." (AP. 64 at page 8-5).

30. Pursuant to section 107(a) of the Clean Air Act, as amended, the Administrator of the Environmental Protection Agency is required to "designate as an air quality control region any interstate area or major intrastate area which he deems necessary or appropriate for the attainment or maintenance of ambient air quality standards." 42 U.S.C. § 1857C-2(c).

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31. Exercising his administrative authority, the Administrator has designated the New Jersey-New York-Connecticut Interstate Air Quality Control Region. The region comprehends most of the Port District, including Bergen, Essex, Hudson, Middlesex, Monmouth, Morris, Passaic, Somerset and Union Counties as well as extensive sections of Connecticut and New York State. 40 CFR § 81.13.

32. Section 107(a) of the Clean Air Act, as amended, provides that "each State shall have the primary responsibility for assuring air quality within the entire geographic area comprising such State by submitting an implementation plan for each State which will specify the manner in which national primary and secondary ambient air quality standards will be achieved and maintained within each air quality control region in such State." 42 U.S.C. § 1857C-2 (a).

33. Pursuant to Section 107 of the Clean Air Act, as amended, the Administrator shall, if a State does not submit an implementation plan, or submits an inadequate plan, and subject to certain opportunities for extension, formulate his own implementation plan to achieve the national ambient air quality standards in the affected part of the air quality control region. 42 U.S.C. § 1857C-5(c).

34. The State of New Jersey has not formulated a plan, satisfactory to the Administrator, to achieve compliance with the federally mandated national ambient air quality standards for carbon monoxide or photochemical oxidants (hydrocarbons) within its portion of the New Jersey-New York-Connecticut Air Quality Control Region.

35. The Environmental Protection Agency on November 13, 1973 promulgated implementation plans for New Jersey

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dealing with carbon monoxide and hydrocarbons as set forth in 38 Federal Register 31388 to 31400. Since that date many changes have been made, most of them postponing dates of compliance. Negotiation between the Federal Environmental Protection Agency and the Department of Environmental Protection is going on to determine whether other changes are to be made. Judicial notice may be taken of the Plan and related materials in the Code of Federal Regulations and the Federal Register.

The State has openly opposed many of the provisions of the proposed plan. There does not appear to be a present intention on the part of the New Jersey authorities charged with air quality control to submit an alternative plan.

36. Since February 1, 1974, when the New Jersey mandatory auto emission testing program went into effect there has been a 20% reduction in carbon monoxide concentration in New Jersey's air. Reporting on this accomplishment, Russell E. Train, Environmental Protection Agency Administrator, praised New Jersey as a national leader in air pollution control. A spokesman for the State Bureau of Air Pollution Control stated that the 20% reduction in carbon monoxide levels brought the content of the contaminant from four parts per million in the first six months of 1973 down to 3.3 parts per million in the first six months of this year. The spokesman said that the improvement in air quality is bringing the State closer to the standards the federal government has told New Jersey to meet by 1977. However, he noted that the State may have to take further steps to reduce air pollution caused by auto emissions to meet the stringent requirement.

There was a similar decline in carbon monoxide concentration in New York City, which does not have an automo-

tive emission testing program. At the Queensboro Bridge, carbon monoxide concentrations were 20.8 parts per million in June 1973 and 15.5 parts per million in June 1974, a 25 per cent improvement. In February 1973, the figure was 15.9, while in February 1974 it was 13.5. On Canal Street, the carbon monoxide reading in January 1973 was 9.6 and in January 1974 it was 7.1. In June 1973 the concentration was 9.3 and in June 1974 the concentration was 10.1. According to an article appearing in the December 3, 1974 issue of *The Star Ledger*, New York Environmental Protection "officials confirmed that auto pollution was less during the period of the gas shortage." The article also stated:

> "Having only 10 months' experience with mandatory emission control testing, and this coinciding with a period of generally curtailed driving because of an energy crisis, neither federal EPA nor [New Jersey] DEP officials can make a convincing case for the experimental program."

III. History of Rapid Transit in the Port District.

A. Prior to 1962.

1. Chapter 591 of the Laws of New York of 1921 created a commission to prepare "a preliminary plan and report, including estimates, for the combination, improvement and extension of existing rapid transit railroads, street surface railroads, and * * * omnibus lines and any railroad used for local service, operating between a point or points within the city of New York and a point or points within the county of Westchester, * * * and for otherwise improving, by new construction or otherwise, the transportation facilities between the city of New York and the county of Westchester."

2. Chapter 104 of the Laws of New Jersey of 1922 established a commission to study and report upon plans for providing a comprehensive scheme of rapid transit between various communities in northern New Jersey and the City of New York. The preamble to the aforesaid act contained legislative findings as follows:

> "Whereas, By act of the Legislature entitled 'An act to authorize a commission to enter into compact or agreement with the State of New York for the development of the port of New York,' passed April seventh, one thousand nine hundred and twenty-one, a commission now exists for the development of a comprehensive plan for the development of said port; and
>
> "Whereas, Said comprehensive plan in its consideration of transportation problems does not include the problem of passenger traffic in the territory covered by said port development plan; and
>
> "Whereas, Said problem of passenger traffic should be considered in co-operation with the port development commission so as to develop an efficient system of rapid passenger transit between the New Jersey municipalities lying within the territory covered by said port development plan and between said respective municipalities and the city of New York."

3. Pursuant to the aforesaid statute and subsequent joint resolutions passed by the New Jersey Legislature, a North Jersey Transit Commission undertook a comprehensive study of the rapid transit needs of a nine county

area of New Jersey. The 1925 report of the Commission stated:

> "... New Jersey must give immediate and thoughtful consideration to its transit problem in order that its growth and prosperity shall be continued and in order that its natural development may not be retarded.
>
> "Already the nine northern counties of New Jersey are confronted with a serious situation and that situation is growing more serious each year.
>
> "If the solution of the transit problem is delayed longer . . . (t)he result would be disastrous to New Jersey.
>
> "This transit problem is one of great magnitude and many complexities. Its solution lies almost as much on the New York side of the river as in New Jersey.
>
> "The State of New Jersey must change the present inharmonious, inefficient and almost impossible transit chaos to a comprehensive, efficient and workable whole that will adequately serve commuters to New York as well as properly build up this section of the State."

The report favorably considered the establishment of a double loop system connecting all the railroads of North Jersey to a direct New York City system running from lower Manhattan to 59th Street.

4. On January 15, 1926, the North Jersey Transit Commission presented a comprehensive plan to meet the mass

transit crisis of northern New Jersey. The 1926 report stated that:

> "Northern New Jersey has an acute transit problem.
>
> "The need for relief is so urgent that temporary measures must be resorted to at once if permanent and more comprehensive plans cannot be carried out in the very near future."

The 1926 report recommended an Inter-State Loop Line, a Meadows Transfer Station, direct rapid transit access to New York City, Hudson and Manhattan Railroad extensions in New Jersey and the extension of New York rapid transit service to New Jersey. (Stip. 66-73)

• • •

7. In 1927 the New Jersey Legislature, stating that it was acting "under and pursuant to the provisions of the [Port Authority] compact," "authorized and directed" the Port Authority "to make such plans for the development of said district supplementary to or amendatory of the comprehensive plan heretofore adopted by the Legislatures of the two States . . . as will provide adequate interstate and suburban transportation facilities for passengers traveling to and from one State to the other within the said district, and from one part of the said district to another, sometimes referred to as commuter or suburban passenger traffic, to the end that travel between the various parts of the port district may be made more convenient, practicable and economical for those residing in one region in the port district and doing business in another region thereof." The Port Authority was also directed to "submit, as a part

of its report, a legal plan for the financing of the said improvements through the Port of New York Authority as the corporate municipal instrumentality of the two States or otherwise." This legislation, which became Chapter 277 of the Laws of New Jersey 1927, was signed by Governor Moore of Jersey and was approved in 1928 by the New York Legislature but was vetoed by Governor Alfred E. Smith, who issued the following statement in support of his veto:

> "NOT APPROVED.
>
> "This bill aims to authorize and direct the Port of New York Authority to study the interstate suburban passenger problem of the metropolitan district with a view to enlarging the comprehensive port plan so as to comprehend suburban traffic relief.
>
> "There can be no question as to the urgent need of working out a solution of the suburban passenger traffic problem in the metropolitan district. The present railroad stations and traffic facilities in New York City, so far as suburban transportation is concerned are already hopelessy inadequate and no hope for the future lies in the efforts to expand these facilities. On the other hand, I am satisfied that no solution can be found by merely dumping suburban passengers at the out'ying parts of the city and forcing them into the already overcrowded city subway and elevated systems. Some solution must be found along the lines of an entirely new suburban subway system through which suburban trains can be operated connecting New Jersey, Westchester and Long Island with New York City

> and with each other. Various attempts to solve this problem have been made through special legislative commissions and through private agencies and organizations. The solution now proposed is that the Port of New York Authority finance these facilities through the issuance of bonds similar to the bonds issued to finance the various Hudson River and Staten Island bridges.
>
> "No one can question my interest in and support of the Port of New York Authority. I was a member of this authority by appointment of Governor Miller between my first and second terms as Governor and represented the authority at Albany when the comprehensive plan for port development was adopted by our State Legislature. I have been and am vitally interested in carrying out this comprehensive plan. It has been a source of great satisfaction to me to see the soundness of the financial principles back of the Port Authority demonstrated in the building of the great bridges which are now under way. On the other hand, it has been a great disappointment to me to find that the opposition of the railroads has prevented to date the making of real progress in working out the program of freight distribution in the port which always has been the main object and purpose of the Port of New York Authority. I am satisfied that the Port Authority should stick to this program and I am entirely unwilling to give my approval to any measure which at the expense of the solution of the great freight distribution problem will set the Port Authority off

on an entirely new line of problem connected with the solution of the suburban passenger problem.

"For the above reasons, the bill is disapproved.

(Signed) ALFRED E. SMITH"

8. The Port Authority's 1928 Annual Report stated:

"In its last annual report, the Port Authority advised that creation of the Suburban Transit Engineering Board had resulted in wholehearted cooperation between the various public agencies of the Port District and the railroads concerned with the problem, and recommended that the cooperative efforts of these associated interests being devoted to a solution of this difficult problem, be fostered and encouraged, and further suggested as a helpful measure to this end, the passage of legislation by the State of New York concurring with New Jersey in its direction to the Port Authority, as contained in Chapter 277, Laws of 1927.

"An appropriate bill to this end was passed by the New York Legislature at the 1928 session but met with the Governor's veto. This failure of this legislation resulted in no funds being made available to the Port Authority for specific purposes of suburban rapid transit.

"However, upon mature consideration, the Commissioners of the Port Authority resolved to continue the Suburban Transit Engineering Board and its support thereof to the extent funds available might permit. The reasons therefor are contained in the following resolution adopted at a meeting of

the Commissioners, June 11, 1928, which provided in part:

"Since the adoption in 1922 of the statutory Comprehensive Plan by the two states, dealing with the transportation of freight, the States of New York and New Jersey have, by various acts, added to the said Plan the building and operation by the Port Authority of four bridges over which passengers are to be carried by vehicles and/or rail;

. . . . .

"The Commissioners of the Port Authority have found in their studies that no adequate or effective interstate transportation development can take place without taking full account of transportation of passengers as well as of freight throughout the Port District;

. . . . .

"At many points in the statutory Comprehensive Plan, problems arise as to which rail or bridge facilities shall be used primarily for freight or primarily for passenger service, and which for both." (Stip. 75-78) • " •

10. On February 27, 1928, the North Jersey Transit Commission issued its annual report for the year 1927. The report recognized:

". . . the growing impatience of the public with the discomforts, indecencies, delays and money losses caused by present means of travel . . . and is prosecuting its work with due regard to the urgency of the problem.

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> "Better transportation for some 350,000 daily commuters between their homes in this state and their work in New York . . . is an acute present problem, the solution of which is vital to the welfare of an army of our citizens."

The report noted "with keen satisfaction . . . a significant achievement during the past year in respect to the commuter problem"—during a conference between the North Jersey Transit Commission and the Commissioners of the Port Authority, "decision [was] reached that the bi-state character of the Port of New York Authority enabled it to function admirably as a co-ordinating agency between the various official bodies severally engaged in the study of the commuter problem in different parts of the Metropolitan District of New York and New Jersey." The report announced the formation of the Suburban Transit Engineering Board (including the Port Authority) to act as a central agency of transit commissions, railroads, and allied state bodies concerned with the problem of commuter transportation. Negotiation between the North Jersey Transit Commission and the Port Authority brought about a contract between the two agencies under the terms of which financial support was jointly provided for the Suburban Transit Engineering Board. The formation of the latter Board permitted the North Jersey Transit Commission to devote its entire effort toward the development of a New Jersey system leaving the interstate problem to the Suburban Board, which included the Port Authority. (Stip. 79-80) • • •

23. In a 1951 report [submitted to Governor Driscoll, L. Alfred Jenny, consulting engineer] traced the history of previous plans to develop rapid transit facilities commencing in the 1890's. Mr. Jenny listed 16 separate plans, including six of his own between 1921 and 1951. Mr. Jenny noted that the 1920 Plan of the New York-New Jersey Port and Harbor Development Commission (the "Red Book") had stated, "Our Port problem is primarily a railroad problem . . . therefor, the comprehensive plan to evolve which this Commission was created is essentially a railroad plan. . . . A complete reorganization of the railroad terminal system is the most fundamental physical need of the Port of New York. . . . The most pressing element of the entire port problem is that of railroad service to and from Manhattan." Mr. Jenny further noted that "although 30 years have elapsed since, and our problem has grown very much worse, we still have done nothing to solve it." Noting that the Port Authority's March 1, 1937 report had stressed the desirability of the development of rapid transit facilities for northern New Jersey, Mr. Jenny stated: "This sound advice was given a decade and a half ago, yet no one has paid any attention to it, not even the Port Authority itself. On the contrary, it has actually worked for more highway traffic, which it had admitted would never solve our problem, and even today, it is talking of building more vehicular facilities instead of endeavoring to do the railroad job it was created to do over three decades ago." Mr. Jenny also noted that on December 1, 1950, a commuter organization of passengers of the Central Railroad had issued a report, following a conference with Port Authority officials, which stated, "The general aim of the Port Authority seemed to be that of avoiding transit problems." In reference to the existing situation he stated:

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> "For three decades we have been making plans, and spending money in an effort to solve this prob-

lem. All we have to show for this effort is a series of partial and ineffective and expensive solutions, and a few overall and coordinated plans. However, none of these have even been accepted as the solution, to say nothing of having any part of these plans effectuated. We are, therefore, no better off today than we were 30 years ago when the two states decided that the problem was so serious as to warrant the creation of an Authority to solve it.

"Today the situation is very much worse than it was 20, or even 10 years ago. Some railroad tracks have been taken up, many trains have been eliminated and in some cases as many as 50% fewer trains are being run than was the case 3 decades ago, while in some instances we only have about 10% as many, or even fewer, trains than we had then. Fares have more than doubled in the meantime, and train speeds have been reduced. Anyone with the understanding of the economic need of these regions must agree that we can not tolerate this condition any longer. We must take positive and effective action.

". . . We must stop trying to solve this vast and serious problem by introducing ineffective and poorly conceived half-way measures, and which always showed a large deficit, and we must undertake the task of solving it in the only and proper manner in which it can be solved. We must provide an overall solution, throughly coordinated, and include therein all possible revenue producing features and arrange the facilities in such a manner that the best possible and maximum use can be made. We must also stop using the poorly conceived projects as a base for

discussion, as has too often been done, and then simply say, it cannot be done. That is a very poor excuse for the past failure to produce the proper facilities." (Stip. 93-95) • • •

36. In the 1958 session of the New Jersey State Legislature, Assembly Bill No. 16 was introduced which provided that the Port Authority would take over and financially develop, improve and operate the interstate rapid rail transportation of passenger traffic between New Jersey and New York. In response to this bill, the Port Authority submitted a statement by its Commissioners on November 24, 1958. In a letter accompanying its statement, the Port Authority summarized its position:

"At the outset we must state, as we have stated repeatedly in the past, that we are unanimously opposed to the adoption of Assembly No. 16 or any legislation which would attempt to involve the Port Authority in any way in the deficits of rail rapid transit.

"Our letters of May 29 and September 11 and the attached statement, all contain detailed facts and figures that completely refute the unsound, impracticable and legally impossible recommendations of Assembly No. 16, which would attempt to direct the Port Authority to take over, finance, develop, improve and operate 'rapid rail transportation of passenger traffic' in the Port of New York District.

• • •

"In our judgment, any involvment of the Port Authority in rapid transit would have disastrous consequences for the people of the two States and for

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their joint heritage,—the Port District of New Jersey and New York. Such involvement would cause the Port Authority to default on contractual commitments which the Port Authority must honor for the continued development of the public facilities of the Port District—land, sea and air—which will require the Authority to borrow over $700,000,000 of capital funds during the next five years. These contractual commitments, made with the express authorization of the two States, involve the following of our facilities:

Elizabeth-Port Authority Piers
Brooklyn-Port Authority Piers
Port Newark
George Washington Bridge
(second level, plaza improvements and approaches)
Washington Heights Bus Passenger Facility
Bergen County Expressway
New York International Airport
Newark Airport
La Guardia Airport
Narrows Bridge
Erie Basin-Port Authority Piers

"In addition, any involvement of the Port Authority in rapid transit could well lead to the destruction of the Port Authority as a useful agency of the two States for the continued development of essential facilities on a self-supporting basis and without burden to the general taxpayer.

"It has been suggested: (1) that the heavy deficits of the New Jersey commuter railroads and the cost

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of developing a new and comprehensive rapid transit system should be assumed by the Port Authority, which could absorb these deficits by use of revenues from its present operations; and (2) that if these rail transit deficits—present and future—proved to be more than the Port Authority's overall revenues could absorb, they could be 'made up' by increasing the existing Hudson River tolls and discontinuing the present commutation rates across the George Washington Bridge and through the Holland and Lincoln Tunnels. It also has been suggested that such deficits could be made up by increasing the charges at Port Authority terminal facilities. Another suggestion calls for a bi-State (New Jersey, New York and Connecticut) subsidy to the Port Authority to make up the operational and capital deficits of rail transit.

"By way of summary of our previous communications and our current statement, we must respectfully submit to your Committees again that:

"1. It is legally, financially and contractually impossible for the Port Authority to assume the railroads' increasingly heavy deficits from all or part of commuter operations, or the cost of developing a new and comprehensive interstate rail rapid transit system.

"2. Even if it were legally and contractually possible, very quickly the assumption of rail transit deficits by the Port Authority, the self-supporting agency of the two States, would cripple and destroy the Authority's credit. It would thereby bring to a halt the program now being carried out by the Port Authority on behalf of the two

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States for the continued development of their essential public marine and inland terminal facilities, airports and interstate arterial systems.

"3. The imposition of the deficit financing of rail transit upon motorists would constitute an unfair tax upon a particular group of citizens. A toll increase to 75 cents for all automobiles, including those of regular commuters, and a corresponding increase for all other users of the Hudson River crossings would be required just to meet the 1957 deficits of the New Jersey commuter railroads. If these deficits were to be viewed realistically to include the financing of rapid transit deficits in New Jersey, New York and, as has been suggested, in Connecticut, the users of the Hudson River crossings, and we presume, other river crossings and turnpikes in the tri-State area, would have to pay a bill for railroad and transit deficits amounting to a sum that might reach as high as $150 million a year.

"4. It is impossible, as has been suggested, for the Port Authority to alter existing contracts for charges to users of Port Authority airports, truck terminals, bus terminals, and marine terminals, in any attempt to impose upon them a part of the rail transit deficits. These charges have been established by leases and agreements which may not be altered unilaterally.

"5. A New Jersey subsidy of the Port Authority for rail rapid transit purposes is a proposal that commuter deficits be paid by the taxpayers.

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We find it difficult to believe that this Legislature would support a bill that proposed that the taxpayers of the State of New Jersey should subsidize Port Authority operation to the extent of from $12 million to $20 million or more a year. Furthermore, the Port Authority would cease to be an effective instrumentality of the two States if it were to become a subsidized agency.

"In the attached statement we set forth our detailed reasons for these conclusions and describe how the Port Authority finances its projects, the way in which the market for its revenue bonds operates, and the projects to which it is committed over the next five years. Our statement also demonstrates the legal and financial impossibility of the assumption by the Port Authority of any or all of the rail transit deficits, and reviews how and why the assumption of such deficits would destroy Port Authority credit.

"To finance Port Authority projects we must sell revenue bonds. The security for such bonds is limited to the revenues which the Port Authority develops and receives from its public projects and from the reserves established from those revenues in accordance with the statutes and our contracts with our bondholders. People will buy Port Authority bonds only so long as they have confidence that our revenues will be sufficient to pay interest and principal on such bonds and create sufficient reserves for protection against contingencies and adverse devel-

opments that might impair the security of the Authority's bonds.

"Under our contracts with our bondholders, the Port Authority's reserves and the revenues from present facilities are pledged and committed. They cannot, as a matter of law and contract, be diverted to the development of a deficit rail transit system or for the underwriting of deficits of the New Jersey commuter railroads."

• • •

"Two results would flow from such continuing subsidy, possibly unanticipated by their proponents, but certainly destructive to the continued usefulness of the Port Authority.

"First of all, prospective investors of Port Authority obligations would conclude that the subsidized Port Authority operation was only a first step in a process of involvement, and that an attempt to divert the reserves and revenues of the Authority would be certain to follow. No investment counsellor who has heretofore advised his clients to purchase Port Authority bonds on the basis of its record of self-support could so counsel them again in the face of this threat. Port Authority interest rates would be forced up at once and at the very minimum certain public facilities, for which commitments have been made with the authorization of the two States, would have to be abandoned because the increased cost of borrowing would put them beyond the possibility of self-support.

"Your Committees well know that the essence of the Port Authority has been its long tradition of non-

political corporate management guided by sound business principles in the operation of public facilities which have been placed on a self-supporting basis. This tradition has been respected by successive administrations of the two States over the past 37 years.

"The Port Authority concept is completely incompatible with a power in the Authority to spend tax monies for the raising of which it would have no fiscal or political responsibility. In the case of tax-supported public facilities, the determination of the many considerations which are involved in their operation properly lie with the taxpayers who pay that operation. The Port Authority mechanism, while dependent on legislative authorization and gubernatorial control, must weigh operating decisions against their legal, financial and economic implications to the Authority. That mechanism, therefore, cannot at the same time fit both a subsidized railroad operation and the operations of self-supporting port facilities. The Authority could not possibly observe two standards of management with respect to its operations. The non-business considerations which are completely correct for setting policy for a tax-subsidized railroad operation could in no event be kept out of the agency's other operations, which would be managed by the same Commissioners and the same administrative staff. Thus, the ultimate result of a subsidy would be to destroy not only the self-supporting financial management of the Authority but also its managerial efficiency."

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37. The following is an excerpt from the statement by the Commissioners of the Port of New York Authority dated November 24, 1958:

> "The Commissioners of the Port Authority are unanimously opposed to Assembly No. 16 and to any other legislation which would attempt to involve the Port Authority in any way in responsibility for rapid transit.
>
> PORT AUTHORITY ASSUMPTION OF TRANSIT DEFICITS IS LEGALLY AND FINANCIALLY IMPOSSIBLE
>
> "This opposition is based on the conclusion of the Commissioners that: (1) It is legally, financially and contractually impossible for the Port Authority to assume the railroads' increasingly heavy deficits from commuter operations or the cost of developing a new and comprehensive rail rapid transit system; and (2) The assumption of rail transit deficits by the Port Authority, the self-supporting agency of the two States, would immediately cripple and very quickly destroy the program of the two States now under way for the continued development of their essential public port and harbor facilities, airports, and interstate arterial systems.
>
> • • •
>
> "In addition to the General Reserve Fund, various special reserve funds have been created as a result of contractual commitments with bondholders in support of the various issues of Port Authority bonds. As in the case of the General Reserve Fund, the Authority may apply moneys in the Special Reserve

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> Funds for purposes relating only to those of its bonds secured by a pledge of the General Reserve Fund, including purposes relating to facilities financed by such General Reserve Fund Bonds.
>
> "All Port Authority revenues not applied to operation and maintenance and debt service *must* be paid into one or another of these reserve funds. There are no excess revenues which are free of this contractual commitment to bondholders.
>
> "Generically, Port Authority bonds may be classified as 'municipal bonds'. However, the vast majority of municipal bonds are general obligation bonds secured by the tax levies of the particular unit issuing such bonds. The marketability of such bonds has little to do with the specific purpose of the particular issue but rests primarily upon the tax record and future prospects of the entire community within the taxing jurisdiction. Unlike tax-supported obligations, however, the marketability of the Port Authority bonds has a very direct relationship to the facilities for which the borrowing is made.
>
> "Moreover, in addition to the revenue prospects of the facility itself, the prospective Port Authority bondholder weighs the financial strength of the Port Authority by an examination of its record of meeting required and anticipated debt retirement, the Authority's reputation for financial management and its record of administration with respect to the ratios of expenses to revenues.
>
> "The factors enumerated above can be determined by examination of the record and simple calculation.

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Not so readily determined and identified, however, is the 'confidence' that the holders of Port Authority bonds have historically demonstrated. Three factors have contributed to this confidence. First, all groups of facilities, including those that were initially deficit facilities, have been brought into the area of complete self-support. Second, the Port Authority has always honored both its express and implied obligations to its bondholders. Third, its management has been characterized by stability and continuity and its financial policies have earned the respect of investors.

• • •

"Late in 1951 the Commissioners of the Port Authority met again with Governor Driscoll of New Jersey to discuss a suggestion which had been advanced that the Port Authority might undertake the financing of an electrified rail transit system between New York and New Jersey. The Commissioners noted the facts developed in the many studies which had been undertaken, including the conclusions of the New Jersey Legislative Committee of 1941, and expressed the conviction that any suggestion that the Port Authority was about to take over or to be asked to take over the interstate rapid transit service would have a most serious effect on its credit.

"The Port Authority Commissioners pointed out that the principle of self-support is the whole strength of the Port Authority's ability to carry forward the programs of terminal and transportation development entrusted to it by the two States on a revenue bond basis; that the Port Authority's

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credit structure would be seriously impaired if there was any implication that the Port Authority was even considering the financing of rail transit; that any amendments to the Port Compact under which the Port Authority would have recourse to public subsidy from tax levying sources in support of its projects would destroy the entire concept and character of the Authority.

"Disastrous Effect Upon Port Authority Credit

"Even if it were possible to ignore the legal and financial impossibility of the Port Authority assuming responsibility for commuter rail deficits as described above, such involvement would have a disastrous effect on Port Authority credit. This statement represents not only the considered judgment of the Commissioners of the Port Authority, but it is supported by views expressed by other responsible persons in the investment and banking field, who as a practical matter, are the controlling influence upon the receptivity of bondholders to Port Authority investment. Their views are uniform that the introduction of rapid transit deficits into the Port Authority's overall financial responsibility would have the effect of seriously impairing the Port Authority's credit standing.

"For instance, Mr. E. B. Rockwell of Halsey, Stuart and Company (co-managers of an investment banking syndicate which consistently bids on Port Authority bonds) wrote to the Treasurer of the Port Authority on July 23, 1958 as follows:

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'In our opinion any assumption of responsibility on your part for rail rapid transit in the New York area would, on almost any conceivable terms, be harmful to the present investment standing of the Port bonds and would adversely affect the ability of the Port Authority to finance in the future on terms as favorable as hitherto. In our opinion, it is most essential for the preservation of The Port of New York Authority to be completely free of any responsibility whatsoever for rail rapid transit in this area.'

"Mr. Reginald M. Schmidt of Blyth and Company (co-managers of another syndicate which consistently bids on Port Authority bonds) also wrote to our Treasurer on July 16, 1958 in part as follows:

'If the Port of New York Authority is to continue expanding its present facilities and other facilities that lend themselves economically to sound revenue bond financing, it would be fatal to the Port's credit if they undertook to finance transit systems by pledging its surplus revenues and general reserve fund.'

"In support of the statements made by these municipal bond experts who both underwrite and purchase our bonds, we quote in part from an editorial from the June 30, 1958 edition of 'The Daily Bond Buyer,' which is the trade paper for municipal dealers all over the country. This editorial stresses the serious effect which transit responsibility would have on the Port Authority's credit.

'One of the few real efforts toward a solution of the mass transportation problem of the New York-

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New Jersey Metropolitan Region has been delayed because the New Jersey Legislature has adjourned until next November, without completing action on the proposed formation of the Metropolitan Transit District. An identical bill was adopted by the New York Legislature early this year and signed by Governor Harriman, but it will take effect only if New Jersey also acts. The measure squeaked by the New Jersey Senate, but the chances of approval by the Assembly are believed to be dim.

'It is regrettable that formation of such a bi-state agency, comparable in some ways to the Port of New York Authority, will be delayed and perhaps defeated in the end. Mass transportation is the universal problem of the "exploding cities" of the United States and many other countries. In the United States it is more formidable than anywhere else. Ever more penetrating studies show that it has some general aspects, but also many that are peculiar to each separate Metropolitan Region.

'The Port of New York Authority has often been assailed for its aloofness, but the Port Authority has excellent reasons and spelled them out plainly early this month in a series of analyses of commuter railroad deficits, the experience of transit systems in other Metropolitan Areas, and the effect on its own credit and activities of any attempt to participate. As to the latter, there are impassable legal obstacles and the financial results would be ruinous. The Port Authority therefore frankly declared that creation of the proposed

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Transit District is the only action that can assure progress this year on the New York-New Jersey transit problem.'

"These statements were made by responsible investment banking leaders. For all practical purposes they are the controlling influences of our credit. We can sell Authority bonds only through these syndicates and on such terms as the syndicates believe are required to make them marketable.

"Obviously, these market analysts would regard any Port Authority involvement in rapid transit as a financial disaster. If the Port Authority can be compelled to assume a deficit operation of any sort, even one not approaching the rail transit deficit in size, investors would have a right to assume that the Authority was becoming the dumping ground for deficit operations of all types. The Authority's credit could not survive such a breach of its investors' present confidence that the Port Authority will restrict its operations to facilities which it believes can eventually be made self-supporting. The importance of this lies in the fact that it transcends arguments as to the size of the present transit deficit. To investors it would make no difference whether the proposal was to force a $2,000,000 or a $12,000,000 or a $20,000,000 annual deficit on the Port Authority. Confidence is the essence of credit and it would be gone.

"Flattering though they may be, suggestions that the Port Authority's 'technical know-how and managerial experience' would somehow dissipate rail transit deficits will not stand serious examination. Nor would prospective purchasers of Port Authority obligations be lulled into disregarding the uniform record of large and increasing rail transit deficits by the mere fact that the Port Authority's 'managerial experience' had been brought into the picture.

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"The impact of a loss of credit would not be limited to the Port Authority's future financing. Outstanding bonds would immediately sell at a discount and the holders of the $500 million of outstanding Port Authority bonds, who purchased them on the assumption that only those facilities would be undertaken which are self-supporting or capable of self-support, would suffer serious losses. At the very minimum this involves a breach of the Authority's moral obligation to these bondholders and one which the Legislatures will want to consider."

38. On January 9, 1959, a joint report on the proposed Metropolitan Rapid Transit District and Port Authority statutes was issued by the New Jersey Assembly Committees on Highways, Transportation and Public Utilities and on Federal and Interstate Relations. The report noted that the MRTC bill did not specifically mention the Port Authority by name as it did other agencies, such as the New York Transit Authority; that the implicit proposal of the Metropolitan Rapid Transit Commission bill to use local property taxes as the primary method of financing "was a wholly unrealistic proposal [as] the municipalities and counties comprising the district . . . are now involved in a substantial effort to find a way to reduce the tax burden on real estate"; the proposed organizational structure of the

Metropolitan Rapid Transit District was "most disturbing" and "provided less control over the Board than exists in the hands of stockholders in a private corporation"; and that supporters of the Metropolitan Rapid Transit Commission plan had come to recognize the many serious defects in the structure of the agency and otherwise. The report also stated that many of those who originally felt that the Port Authority should undertake the entire mass transit obligation had come to realize that in light of all the circumstances that could not be justified at that time. The report further stated:

> "There can be no question that the carrying on of a transit function was well within the Port Authority Compact terms and well within the present powers. However, two extremely important factors mitigate against any present assignment of the task to the Port Authority by law. First, as of now no one can say with certainty what the size of an operatinp deficit would be. While the Port Authority no doubt could undertake an activity which would involve a deficit—even a permanent one—it could only do so if there were real assurance that the size of the deficit would be such that there could be no doubt of its ability to absorb it. As pointed out by the Supreme Court in the *Weehawken* case, 14 N.J. 570, the design of the Port Authority rests on two concepts: that by a pooling of facilities in one agency, activities which by themselves could not succeed financially could be undertaken, and that the aggregate pooled operation of all facilities should be self-supporting. It is this last factor that mitigates against A-16. If there were sufficient assurance that

> the aggregate operation would continue to be self-supporting, and sufficiently so as not to tend to impair or adversely affect the efficiency or credit of the Port of New York Authority, it would be a question of policy for the Legislature to decide whether to assign to the Port of New York Authority a function that would make it more expensive to borrow money. The committees are satisfied that this is the context in which Mr. Tobin's testimony that the Port Authority could not, legally or financially, undertake commuter operations, must be read. The same comment is to be applied to the Memorandum of Understanding between MRTC and the Port of New York Authority. There can be no doubt of the propriety of assigning a transit function to the Port Authority if there were proof of an adequately clear and convincing nature by competent estimates that the predictable deficits of the transit operations would be sufficiently less than predictable net revenues from other operations as not to impair existing contractual obligations with bondholders or the overall ability, credit and efficiency of the Port of New York Authority. Evidence of this kind was not presented, nor can it be until there is formulated a general plan with sufficient detail. At that time, reasonably reliable estimates will be possible, and the Legislature can then determine whether and to what extent the Port of New York Authority should be directed to undertake a major operating or financial role in its effectuation. The concept of a transit district agency was accordingly agreed upon as the most suitable one to accomplish the task.

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"At the same time, it was felt that the Port Authority should give the district every conceivable aid that might advance its work, and the substitute bill expressly so provides. We have no doubt that the Port Authority can be of tremendous aid and it is in the public interest, as well as in the proper discharge of its own duties that it will provide it wholeheartedly. In addition, it is conceivable that some kind of Port Authority participation in some part or parts of the plan is desirable and feasible without requiring it to assume the entire deficit. This is most likely to take the form of planning, constructing and financing some of the essential facilities. Some of them may even be modest deficit operations of a predictable nature, such as parking facilities at junction or transfer points, at rail line stations, or more substantial ones such as stations, interconnections, bridges, tunnels and the like, with the assurance, however, that Port Authority contractual obligations to bondholders and overall efficiency and credit would not be impaired. It may even be able, at the start, to provide office space for the district so that it may get quickly under way.

"At the emergency and interim stages, it is clear that implementation, in the sense of actual operation, should continue to be by the railroads and other carriers. The district will serve as a focal point or integrating device through which all arrangements may be made. Conceivably, it could arrange for issuance of the passenger tickets for use on the commuter network, if that should offer any cost-saving advantage. Beyond these two stages, however, no one can predict what assignments should be made.

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Implementation of the more permanent general plan will need to await the experience obtained from the interim plan and the design of the general plan itself. The substitute bill is drawn to provide all needed flexibility."

39. By Chapter 13 of the Laws of New Jersey of 1959 and Chapter 420 of the Laws of New York of 1959, the States of New Jersey and New York entered into a compact with the consent of Congress. Public Law 86-302; 73 Stat. 575 (1959). The compact created the New York-New Jersey Transportation Agency as a body "corporate and politic" which would "serve as a public agency of the states of New York and New Jersey in dealing with matters affecting public mass transit within and between the two states." §3.1. In entering into this compact, the Legislatures specifically found:

"Provision for efficient and proper transportation of commuters and other persons by public transit methods within the New York-New Jersey metropolitan area is essential in the public interest.

"Recent trends toward decay of existing systems, particularly in respect to transportation services crossing the Hudson river, have created a condition of impending emergency requiring prompt action on an interim basis for the establishment of an operating system designed mainly on the best use of existing facilities and equipment at the least financial hardship upon the operators thereof consistent with public needs, pending the development of a proper and acceptable general plan.

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"Present uncertainties as to the nature and extent of any acceptable and feasible general plan, as well as to the capital and operating cost of the same, require that such questions be inquired into upon the basis of experience accumulated in the operation of an interim plan. The preparation and execution of an interim plan as well as the preparation of a general plan can and should be accomplished by a metropolitan transit district to serve as a regional agency of the States and to have the full assistance, support, co-operation and participation by all persons and agencies, private and public, of any 1 or more of the States within the proper limits of its own functions and duties." (Stip. 110-126) • • •

40. On September 21, 1959 by Public Law 86-302, 73 Stat. 575, Congress, pursuant to a joint resolution, consented to the Compact entered into between the State of New York and the State of New Jersey for the creation of the New York-New Jersey Transportation Agency. The congressional consent provided:

(a) The right to alter, amend, or repeal the joint resolution was expressly reserved.

(b) Any long-range plan, when adopted by concurrent legislation of the compacting states, shall be submitted to Congress for its consent before such long-range plan becomes effective. (Stip. 127) • • •

The Compact provided that the agency was to continue in existence until June 13, 1961, but that its existence could continue thereafter as concurrent legislation might provide (Article 4, §4.6). In 1961 the Legislatures of both States

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extended the agency's duration to June 30, 1966. Ch. 55, Laws of N.J. 1961; Ch. 273, Laws of N.Y. 1961. There was no subsequent legislation extending the existence of the agency beyond 1966.

41. By Chapter 25 of the Laws of New Jersey of 1959 and Chapter 638 of the Laws of New York of 1959 the Legislatures of the two States provided that "upon the election by either State . . . the Port Authority shall be authorized and empowered" to purchase and own railroad cars for the purpose of leasing them to commuter railroads within the electing State. The statutes expressly prohibit the Authority from borrowing money for the purchase of such cars until the electing State has guaranteed payment of both principal and interest on the obligations issued for that purpose.

New York immediately chose to have the Port Authority proceed on its behalf to purchase railroad cars for lease to the commuter railroads of that State. Ch. 639, Laws of New York of 1959. Pursuant to this program, as later implemented by a 1961 New York constitutional amendment, the Port Authority has presently outstanding over $90 million in New York State-guaranteed railroad car bonds and has purchased for lease to commuter railroads within the State 467 air conditioned passenger cars and 8 locomotives. 1972 Port Authority Annual Report, 15. The State of New Jersey has not taken legislative action to participate in this commuter car program.

42. By Chapter 14 of the Laws of New Jersey of 1959, a Division of Railroad Transportation was created and established as a part of the State Highway Department in order to improve rail transportation in the State. The Legislature found:

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"(a) Many of the railroads serving this State are seeking to curtail or eliminate much of their commuter and passenger railroad service.

"(b) Railroad transportation is the most efficient means of moving large groups of people in a short space of time such as is necessary, particularly, during the rush hours at the commencement and close of each working day.

"(c) Adequate commuter and passenger railroad service throughout the State is essential for the welfare and prosperity of the people of the State.

"(d) It is therefore imperative that the State lend its assistance in seeking a solution to the problems confronting the railroads in connection with commuter and passenger service and to insure continued operation of adequate commuter and passenger railroad services." (Stip. 128-130) •••

47. In 1960 the New York City Transit System had an operating deficit in excess of $20 million, exclusive of annual debt charges of $87 million which was subsidized by the taxpayers of New York City. The aggregate deficit from commuter operations of the New York Central, New Haven, Long Island Railroads and Staten Island Rapid Transit Railway was estimated at between $10 million and $15 million annually for the year. New York City taxpayers' subsidies of the Staten Island Ferry operations were approximately $6 million. Thus, in 1960, the total of commuter railroad and rail transit deficits in the New York-New Jersey area approached $128 million of which $87 million was for capital debt charges.

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48. On January 1, 1962 the Division of Railroad Transportation, New Jersey State Highway Department, issued its Second Annual Report and Recommendations entitled "Will We Emerge?"

> "The rail carriers' 'illness' has become a progressive one, reaching a crisis in the last decade. In our own State, as in some other sections of the country, railroads were caught in a squeeze between rising costs and declining income. The State and the municipalities have been reluctant to allow the railroads to be relieved of property taxes. Grandiose plans developed by worried officials, numerous traffic consultants and private groups have also been ineffective. The Public simply was not convinced that the situation was serious enough to warrant the expenditure of the hundreds of millions of dollars most of the transit plans required."

THEN AND NOW

"The Public's attitude appeared to be 'Why worry?' It was easier and more 'entertaining' to complain about transit deficiencies than to do something about them before they became a serious menace.

"New Jersey railroads grasped at a 'last, drastic remedy' for survival. In an attempt to avail themselves of the advantages of the Federal Transportation Act of 1958, some lines applied to be relieved of passenger operations, specifically commuter service. Unless this could be accomplished, they warned, they would have to go out of business.

"Realizing that loss of rail commuter service would be a blow to our State's economy far more serious

than any natural catastrophe yet experienced, our State Administration determined to do something about assisting the railroads. Prior attempts had met with general public apathy, and even antagonism in some quarters. The 'sins of the father'—dating back to some of the early railroad promoter tycoons —had left their imprint on the public mind.

TRANSPORTATION DIVISION

"Accordingly, a Division of Railroad Transportation was created within the Highway Department and given a two-fold task—to preserve essential rail service and to improve it where possible. The New Jersey commuter crisis of 1958-59 created a problem which could not be 'put on the shelf' as had been the practice over the years. The New Jersey Highway Department, possessing a background of experience with transportation in its broadest sense, knew full well the futility of even attempting to accommodate the tremendous volume of this 'Corridor State' on its existing highway system.

"The first stage of the project—a 'stop-gap' action only—has been accomplished. The State contracted with the carriers for continuation of essential passenger service for the fiscal year 1960-61 and again, without any appreciable fare increase, until August 29, 1962.

SERVICE ASSURED

"Rail transportation for our citizens has thus been assured by contract payments—subsidies, if you will. A definition of subsidy reads: 'A government grant

to a private enterprise considered of benefit to the public.' The action taken and the incentive could not be better expressed.

"The Highway Department, cognizant of its responsibility for the movement of people and of goods by all available means of land transportation, has to date furnished some twelve million dollars from road construction funds for this purpose.

"Had the Department not made this sacrifice of the equivalent of two miles of highway (average cost of N.J. modern highways is $6,250,000 per mi.), it would have been faced with a shut-down of rail passenger service and the impossible task of making immediately available adequate highways to accommodate an additional 266,000 passenger trips daily. This just couldn't be done, either from the standpoint of funds or time.

• • •

"After a considerable period of successfully avoiding all attempts to involve it in rail transit, the Port of New York Authority was finally persuaded by our Division of Railroad Transportation to assume the acquisition, rehabilitation and operation of the H & M, even though the revitalized line might fail to record a profit. The Authority still resisted extending its operations beyond H & M's main stem necessitating further forceful negotiations before extensions and rail transfer stations were included.

"Rehabilitation of this vital interstate commuter facility must be assured before other programs outlined herein can be initiated. It would be the height

of folly to proceed with such improvements without first taking this essential step.

"The Port of New York Authority, its fiscal structure maintained by income from tax-free vehicular crossings of the Hudson River largely at the 'expense' of rail transportation, is the proper agency to rehabilitate the H & M and provide suitable extensions to connect it with other North Jersey commuter railroads. The Division is negotiating terms of necessary legislation with the State of New York and the Port of New York Authority to accomplish this."

B. Acquisition of the Hudson and Manhattan Railroad Company by the Port Authority

1. In 1908, the Hudson and Manhattan Railroad Company, a privately-owned concern, began operating a railroad facility between Hoboken and Manhattan. Service between Hudson Terminal and Jersey City commenced in 1909 and the service was extended to Newark in 1911. The Railroad was in financial difficulty for many years, and although formal bankruptcy proceedings against it did not commence until 1954, the Railroad was insolvent from the early 1930's.

2. In 1959 the United States District Court for the Southern District of New York approved a reorganization plan which left the company with enough cash to continue operations for two years but without funds to provide needed capital improvements. *In re Hudson & Manhattan R.R.*, 174 F. Supp. 148 (S.D.N.Y. 1959), *affirmed sub. nom. Spitzer v. Stichman*, 278 F.2d 402 (2d Cir. 1960). (Stip. 136-140). • • •

3. In 1960, the New Jersey Senate created a bi-partisan committee under the chairmanship of Senator Frank S. Farley (the "Farley Committee") to conduct "a full and unlimited investigation" of the Port Authority. The Committee was authorized and directed to study "the entire financial structure and operations" of the Authority and to determine "whether or not the said Port of New York Authority is fulfilling its statutory duties and obligations." (Senate Resolution No. 2, 1960; Senate Resolution No. 7, 1961)

4. During the Farley Committee hearings, Dwight R. G. Palmer, New Jersey State Highway Commissioner, testified on January 26, 1961 in part as follows: (Stip. 141-42)
• • •

"There has been a multiplicity of studies, countless commissions and associations engaged in surveys of our metropolitan areas. A perusal of these reports impresses one with the great detail and statistics of the majority of the reports. The supervisors of such compilations undoubtedly were sincere and felt they were pursuing the proper course and yet, years after all these facts were presented, we find ourselves about to go 'down the drain' trafficwise.

"Most of these plans proposed expenditures that staggered the imagination. The likelihood of ever converting such plans into 'pay dirt' and a practical solution had about as much chance as would the financing of Captain Stormfield's visit to Heaven, as described by Mark Twain.

"So, gentleman, in 1959 our commuter problem was brought into sharper focus by the action of the U.S.

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Supreme Court permitting the New York Central Railroad to discontinue ferry service from Weehawken to Manhattan. This same year a rush of service curtailments and fare increase petitions flooded our regulatory agencies and one of our busiest New Jersey commuter railroads posted notice that all service would be discontinued.

"Governor Meyner then assigned the problem to me, first directing my associates and me to provide vehicles of transportation for those 3,000 odd commuters that otherwise would have been stranded when the Weehawken ferry shut down. Within a few months our Legislature responded by establishing the Division of Railroad Transportation. We had adopted a new philosophy; that the job of the Highway Department was one of moving people and goods —not just providing highway alignments for vehicles to travel. This concept was the keystone of the integration of transport facilities in New Jersey, for we recognized that the suburban railroads were essential allies of the Highway Department in meeting the daily peak travel demands of our citizens. We had not worked long with the problem before we realized that the essential ingredient needed to aid in the solution of our problem was money. Conscious of the general rejection of the Metropolitan Rapid Transit Commission plan to tax real estate to meet deficits in its proposals, we developed a different approach. An examination of the operation of the New Jersey Turnpike indicated the availability of sufficient surplus funds to take care of rail transportation difficulties as well as other transport needs, and do this after meeting commitments to all holders of Turnpike

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securities. However, the public decreed otherwise and denied to us the use of these funds. After the defeat of the referendum we reviewed our studies of the rail passenger situation. The results of these studies were set forth in detail in our report to the Governor and Legislature dated April 4, 1960. This report recommended that in order to forestall a complete breakdown of rail services that the carriers be placed under contracts to operate specified trains at established rates. The contracts, we hoped, would assure a continuity of service for our citizens even though they were considered a 'temporary expedient' to be pursued, say, for a period of three to five years, during which time a long range improvement plan could be put into effect.

"Legislation enabling such contracts was introduced in the Senate in May of 1960. It was passed with dispatch in both houses, the legislature exhibiting a keen understanding of the problems and the seriousness of the consequences should the State fail to take action to ease the financial burdens of the rail carriers.

"In the north metropolitan area our recommendations included consolidation of the Jersey Central and the Pennsylvania passenger services over the New York and Long Branch operating the trains through to Pennsylvania Station, Manhattan and a rerouting of all the main line service of the Jersey Central to Penn Station in Newark. Certain of these suggestions are still under study. We also recommended that the Port Authority play a significant part in improving the facilities for the interstate

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movement of our citizens. In this regard I am fully aware that there are those who suggest that the Port Authority should take over the financial responsibility and deficits of all commuter railroads in New Jersey and New York even at the risk of jeopardizing the Authority's credit standing and depleting its reserves below levels set by indenture agreements.

"Considerable time has been devoted to reviewing the Port Authority's capabilities, as well as responsibilities, insofar as commuter rail transit is concerned. Our conclusion as stated in the April [1960] report was that:

'The Port of New York Authority should not, in our opinion, be handed New Jersey's rail problem, nor should it become responsible for the New York subway system or for rail transportation for Westchester or Long Island. We are certain however, that the interstate aspects of the rail movement of persons and goods such as purchase and lease of new Hudson and Manhattan commuter cars and the purchase of the existing interstate railroad ferry boats, do come within their obligations. The foregoing fully recognizes the importance of maintaining the Port of New York Authority's commitments and credit requirements.'

"In other words, we became convinced that the Port Authority's responsibility in the rail transit field should be concerned principally with the interstate aspects of the problem as the Authority is an interstate or bi-state agency. Our recommmendations were consistent with that philosophy.

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"I arrived at this conclusion relying on years of experience in private enterprise. My career has been one of a business man in the industrial field where the courageous survived—where the complacent were left behind and where competition took care of the rest. I have had responsibilities of meeting a payroll—a payroll that each year sought to improve the standards for our workers—and to satisfy the demands of shareholders also. The Port Authority in my opinion must make money and accumulate reserves for the rainy day if it is to be equipped to meet the needs of our two states of New York and New Jersey. It does not have general taxing powers. Its only taxes are the tolls it collects from the users of its facilities. Its shareholders are the public, you and I, and the institutions that buy the bonds. Since the cost of financing often determines the feasibility of a project it stands to reason that you and I get more for our toll dollar in the way of modern and safe facilities if we make certain that the credit rating of the Authority remains intact. Now let's talk specifics for a moment. The Authority has sizeable revenues and reserves today. While I don't have the 1960 figures, reports are that gross revenues in 1959 totaled $105 million and the several reserve funds totaled $71 million. Now as soon as 'reserve funds' are mentioned it is assumed by some that such reserves are 'available' or uncommitted. Such is not the case. These revenues and reserves are pledged and committed by contract to the investors in Port Authority bonds as security for the re-payment of those bonds and for contingent liability in connection therewith and they

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may not legally be diverted. For instance, to strengthen its credit position the Commissioners of the Authority have adopted a policy to commit retention of reserves in an amount equal to two year's debt service. The $71 million in all Port Authority reserve funds at the end of 1959 was just about equal to the following two year's debt service on all bonds. The Authority is required to hold in reserves 10% of its outstanding indebtedness—this amount at the end of 1959 was $57 million. Such revenues and reserves cannot be regarded as uncommitted funds. Diversion of these funds moreover might jeopardize the carrying out of future work authorized by the Legislatures of New Jersey and New York by inviting higher financing costs. Certainly the consequences of such an effect, from the standpoint of the growth and prosperity of this area, must be carefully considered.

"The matter of the pooling of net revenues from all the Port Authority's facilities, as authorized by the Senate in 1931, has received some attention of late. By pooling the revenues, a credit base was established to facilitate financing of projects like the bus terminal serving New Jersey commuters, the third tube of the Lincoln Tunnel, the Hoboken Piers, Port Newark, Port Elizabeth and Washington Heights Bus Terminal which will principally serve New Jersey commuters. Indeed, it is the pooling of such revenues, as I see it, that will permit financing the purchase and rehabilitation of the H & M Railroad. It is clear to me that the action of the New Jersey and New York Legislatures in author-

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izing the pooling of Port Authority revenues and the creation of reserves has made it possible to provide many public transportation facilities that we may not have had otherwise. With the needs for expanded and additional transport projects rearing up in every direction it seems that the principles which enabled the Authority to accomplish so much in so short a time and so efficiently should prevail.

"Now most of us realize that the matter of credit is not an exact science. The credit of an organization depends on quite a few factors; past performance, efficient management and caliber of personnel and markets for the product the institution has to sell; and last but not least—what investors think of the operation as a financial risk. It is, in the final analysis, the practical assessment of being repaid money that they lend to it. This latter reason, I am certain, is why the Port Authority last September, in presenting to this Committee the plan to acquire the Hudson and Manhattan Railroad, talked in terms of what might be done rather than to state positively what would be done. You will remember that they said the Port Authority might be able to sell bonds for the acquisition and modernization of the Hudson and Manhattan Railroad and at the same time continue the financing of the States' vital port development programs, provided investors could be given assurance that investments in rail transit matters would be limited. The Authority also wanted assurance that the key recommendations in our April report would materialize and pointed out that fair financial terms for both the purchase of

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the H & M properties and the Pennsylvania Railroad operating agreements must be obtained. As I see it from my personal point of view acquisition of the H & M is a must. All our plans hinge on it. To insist on terms unacceptable to investors or terms that invite high interest costs might cause delays that will render our efforts 'too little and too late.' It gets down to how badly we need the H & M—do we want it on the investors terms or not at all—it seems to me it is almost as simple as that.

"The H & M railroad provides a vital link in our interstate transport network. It is essential to both states that it not only continue but that it be rehabilitated to more conveniently serve our citizens. The cost of purchase, renovation and a new fleet of cars may be over $80,000,000. The H & M is in the last phase of reorganization, that when accomplished, will separate the Manhattan Real Estate from the Railroad properties. The reorganization document now before the I.C.C. provides that sufficient cash be transferred to the separated Railroad Company to permit normal operation for a period of only two years. Extraordinary demands on its resources such as a prolonged strike, would substantially shorten the period it could operate without public assistance. We did not include the H & M in our contract program because of its interstate nature. We have insisted that it be put under bi-state regulation and that its rehabilitation be a bi-state venture. The Port Authority is the logical agency to do this—it has agreed, as just outlined.

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"I feel certain that you gentlemen of the Legislature have been and will be increasingly in touch with our transportation needs. I am also convinced that the Port Authority's responsibilities will be better met by preserving a sound credit base. (Stip. 142-48) • • •

"Q. By Senator Farley: And taking a hypothetical case—if perchance the Port were in a position financially to handle the commuter service, what would happen to the railroads involving passenger and freight service in this particular area of northern New Jersey? Would they go bankrupt?

"A. Well, the Port Authority has gone on record as feeling that mass transportation's maintenance is absolutely essential. That is contrary to some of the references that I have seen recorded. The Port Authority in itself, with its bridges and its tunnels, and its H & M could, under no circumstances in our considered opinion—although we are not experts, sir—meet the needs of our State insofar as transportation is concerned, and in our opinion their efforts should be confined to the bi-state, interstate aspects, and we, with the carriers themselves, energizing the assistance in each state, would not certainly from our state interest in the Port Authority wish to see them engage in taking over the Long Island Railroad, the New Haven that comes into Manhattan, and the New York Central with all the extentuating circumstances. (Stip. 149-50) • • •

"Q. By Senator Dumont: Commissioner, when the Port Authority made its proposal in September,

at our hearings then, to take over the Hudson & Manhattan Tubes, they surrounded their proposal with certain restrictions which, so far as I could tell, were designed to eliminate any real obligation on the part of the Port Authority beyond taking over the Hudson & Manhattan Tubes, at least so far as the railroad field was concerned. Do you consider those restrictions that they surrounded this proposal with as reasonable ones?

"A. Yes, I do. And I have so stated in my proposal and I do it purely on the basis of what experience I may have had in the field of finance and industry, and of what we are hoping to obtain and acquire in the future in the expansion of facilities that the Port can supply.

"Q. So that you feel if they were to carry out this proposal and purchase the Hudson & Manhattan and do all the rehabilitation that's necessary, they would be doing a, shall we say, satisfactory job, at least in your opinion so far as carrying out their obligation in the railroad field?

"A. I would say this: 1. That they would be doing a fabulous job and accomplishing something that has been talked about for 40 years and which no one as yet has had the courage to tackle and which now is within our grasp. My feeling also is this, in talking with various Commissioners and talking with people in the financial district, that this is not a decision of the Port Authority as such, of a rebellion against going further into transportation, but of the investor, you and I if you will, although we are not

investing this morning whether or not we are willing to loan money to finance obligations that have such distressing characteristics as the present situation. And even the Hudson & Manhattan, which some believe can be brought into a position of profit, which with what little I know I greatly doubt,—it is presently contemplated that there will be a loss of at least some $5 million a year in that operation, and probably a total laying in of risk capital of some $80 million. And it seems impossible, from all of my direct—and not through any other channels —direct contacts, to observe that money could be loaned for even the acquisition of the H & M in the event there was not some assurance that this just wasn't one bite of the cherry and that further transportation business was all to be pulled together. I think it's simply a question of whether the investor says yes or no and at the present time my observation is that the investor says no unless he has that limitation.

"I think, so far as the Port Authority is concerned, that [if] the State felt that they wanted to guarantee the bonds, the investor's bond, then the investor, of course, would be tickled to death to do it. And I think that their capabilities and efficiency are perfectly adequate to even tackle such an encumbrance as this whole transit situation."

5. The following is an excerpt from the testimony before the Farley Committee on January 26, 1961 of E. T. Moore, then President of the Central Railroad of New Jersey:

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"The Port Authority should be just as willing to promote and help to retain essential freight and passenger rail transportation as they are to promote highway and air transportation. The Port Authority is currently sponsoring a study, with the cooperation of railroads, for the consolidation of the railroad marine operations and if this study indicates that such a consolidation is economically sound and in the public interest, the Port Authority should assist in bringing it about. I believe, however, it would be most unwise to expect the Port Authority to take over the whole burden of mass transportation in the New York metropolitan bi-state area.

"The Port Authority, historically, has had the obligation of providing bridges and tunnels for a convenient crossing of the Hudson River. Their extensive facilities have syphoned the profitable portion of this trans-Hudson traffic from the railroads who originally provided the sole means of the river crossing. They should now take the unprofitable with the profitable and assume their full obligation of providing whatever facilities might be essential in the public interest to transport people and vehicles across the Hudson between New Jersey and New York in the metropolitan area. The Port Authority should unquestionably acquire and rehabilitate the Hudson & Manhattan Railroad, which would eliminate the need for antiquated ferry service which is expensive to operate and does not meet present-day transportation needs."

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6. Port Authority Commissioner James C. Kellogg testified at the Farley Committee hearings at the request of and on behalf of all of his fellow Commissioners. The following is an excerpt from his testimony on January 27, 1961:

> "On November 24, 1958, the Commissioners, appearing before a joint hearing of two Committees of the New Jersey General Assembly, submitted a rather complete outline of our views of the rail commuter transit problem and transit deficits. We reviewed the Port Authority's continuing studies of the rapid transit problem in this bi-State metropolitan area over the past thirty years and we submitted a summary of the experience of other metropolitan areas in dealing with their own transit problems. Our report also reviewed the reasons why the Commissioners had no choice but to be unanimously opposed to the adoption of any legislation which would have attempted to involve the Port Authority in the deficits of commuter railroads and rapid transit without limitation or other assurances.
>
> "At the outset, I would like to re-affirm our view that both rail and highway transportation are essential to the economic welfare of the people of the New Jersey-New York metropolitan region. It was for this reason that the Port Authority made $800,000 available to the Metropolitan Rapid Transit Commission to undertake a comprehensive interstate transit survey. We do not now, nor have we ever regarded arterial highway or our own bus terminal services for the accommodation of New Jersey commuters as substitutes for a program of maintaining

and improving rail passenger facilities between New Jersey and Manhattan and throughout the Port District.

"No single one of these programs is a substitute for any of the others since each is important in handling various types of passenger traffic at different times of the day and of the week. An analysis of the relative numbers of passengers using the various modes of trans-Hudson transportation clearly illustrates this point. The automobile plays a significant role in the handling of trans-Hudson passengers on week ends and in non-commuting hours, as it does throughout the nation. The great importance of the common carriers in trans-Hudson commuter transportation becomes apparent, however, from an examination of the relative passenger volumes during the rush hour each weekday. In that hour only 15 per cent of all trans-Hudson passenger movement to Manhattan is by automobile, and more than half of these automobiles are destined for points other than the central business district of Manhattan south of 59th Street. The balance of this peak-hour traffic into Manhattan, 85 per cent, is handled by mass transit—that means railroads and buses, with 46 per cent of the passengers served by rail and 39 per cent by bus.

"Thus, there is no question that rail services are of extreme importance in terms of commuter travel. At the same time, as we suggested to the Legislature in 1958, an attempt to solve the problem of improving commuter rail facilities would be of no value if it were to result in the destruction of the ability of the

Port Authority to continue its comprehensive program of providing, on a self-supporting basis, the indispensable modern port, transportation and terminal facilities. For without these essential facilities, the Port of New Jersey-New York could not continue its predominant position and assure the future prosperity of its people.

"For more than thirty years, the Port Authority has been engaged in studies of all aspects of terminal and transportation facilities and services within the New Jersey-New York metropolitan area. We have continuously searched for solutions to the commuter railroad problem in the form of physical plans which could adequately serve the commuting public and which, at the same time, could be developed on a self-supporting basis. These studies and our conclusions have been submitted to the Legislatures of the two States. No formula for making commuter railroads self-supporting in this area or in any other metropolitan area throughout the country, has ever been found either by the Port Authority, any other public agency or the railroads themselves. All of these studies of rail transit inevitably have concluded that their operation and improvement involve large deficits and that public financial assistance or subsidy is the only method of continuing these critical public services.

"There is universal agreement that essential commuter railroad services must be maintained. For New Jersey and New York, the years 1959 and 1960 were highly significant in the long history of the problem. For the first time, public assistance to all

the Port District commuter railroads has been forthcoming through constructive programs developed in both States. In New York, programs providing for tax relief and for new commuter cars for the New York railroads are in force, and Governor Rockefeller has just announced a four-state program to keep the New Haven Railroad in operation. In New Jersey, a total of $6,000,000 of State funds in the current fiscal year has been appropriated for allocation to the commuter railroads under annual service contracts which guarantee the continuation of this State's essential railroad services.

"In contrast, however, the Hudson and Manhattan Railroad, the interstate rail transit link, has been excluded specifically from the programs of both States for financial assistance to the railroads. Yet it has been experiencing the most serious financial difficulties. Indeed, it is now emerging from bankruptcy under a plan of reorganization which makes it doubtful that the railroad could remain in operation for more than two years.

"The Port Authority always has maintained that the H&M must be kept in operation. This railroad handles more than 31 million passengers a year. Of its 55,000 daily passengers in one direction, it regularly carries about 35,000 New Jersey commuters to and from Manhattan during the peak periods each day.

"At the opening of these hearings, Commissioner Dwight Palmer, on the basis of his intensive studies of the commuter problem, outlined his transit pro-

gram for the State and his own conclusions and those of his Division of Railroad Transportation with respect to the possibility of the Port Authority's participation in meeting the interstate portion of the problem in the light of both the Authority's financial capacity and the limitations of its credit.

"In his April 1960 report to Governor Meyner and the Legislature, Commissioner Palmer stated that 'The Port of New York Authority should not, in our opinion, be handed New Jersey's rail transportation problem, nor should it become responsible for the New York subway system or for rail transportation for Westchester or Long Island.' At the same time Commissioner Palmer urged that the Port Authority and the Division of Railroad Transportation work out some plan through which the Authority would be able to participate in some aspect of the interstate commuter rail problems, expressing his complete understanding that such Port Authority participation must fully recognize 'the importance of maintaining The Port of New York Authority's commitments and credit requirements.'

"In his statement at the opening of these hearings, Commissioner Palmer reviewed the testimony given before this Senate Commission on September 27, 1960 by our Executive Director who had been authorized by the Commissioners of the Port Authority to review with you the progress on the studies and proposals for possible purchase, reconstruction and operation of the H&M by the Port Authority that have been under consideration by Commissioner Palmer and our staff throughout the past year.

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"Commissioner Palmer pointed out that the revenues and reserves of the Port Authority have been pledged in accordance with the statutes of the two Legislatures and that they cannot legally be diverted to purposes over and beyond those specified in its bond covenants and guarantees.

"We were gratified, however, to be able to advise this Commission last September that, within the framework of these outstanding covenants and guarantees, we have been able to suggest certain legal and financial assurances which, if adopted by the Two States, might make it possible for the Port Authority to acquire, modernize and operate the H&M. We advised you at that time that the Port Authority would go forward immediately with a full-scale study of all aspects of this proposal with the hope that such a study could be completed by the end of 1960.

"My fellow Commissioners have requested me to give you a report on the tentative conclusions of this study. I might say that the study has been undertaken on a top priority basis by the Port Authority staff with the assistance of the consulting engineering firm of Coverdale & Colpitts. One of their partners is here today.

"During the course of the study, our staff consulted with the Division of Railroad Transportation in the New Jersey State Highway Department and its counterpart, the Office of Transportation in the State of New York. We also discussed and reviewed various phases of the study with officials of the Jersey Central, Pennsylvania and Erie-Lackawanna Railroads. We consulted throughout the study with

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officials of the H&M and made numerous and detailed inspections of its entire system.

"Our studies confirm what the Trustee of the H&M has stated about the 'antiquated and inefficient' facilities and the 'worn out' rolling stock and other equipment of his railroad. A large and costly capital improvement program therefore will be necessary to bring the bankrupt H&M to proper standards of efficient and reliable service. The H&M has suffered from the same economic and technological changes in the American transportation system that have adversely affected every other commuter railroad in the country. Despite repeated fare increases, these changes have brought about abandonments, service curtailments, neglect and deterioration of plants and equipment—equipment that has long since been depreciated on the books of the railroad companies and that normally would have been scrapped many years ago.

"It is not surprising, therefore, that the H&M, including the railroad, terminal and real estate properties, valued by the Securities and Exchange Commission less than a year ago at $20,500,000, will require on the basis of our studies, a total capital expenditure of about $63,000,000 for rehabilitation and modernization of the plant and for purchase of new cars. This does not include the cost of acquiring the properties. If this $63,000,000 improvements expenditure is made, we believe that the public will enjoy comfortable, modern and reliable rail transit service across the Hudson River.

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"I would like to outline briefly what the Commissioners of the Port Authority believe can be accomplished for the H&M passengers: (1) if the Legislatures of New Jersey and New York enact the legislation which would make it possible for the Port Authority to finance such a project; (2) if it is possible to acquire at a fair and realistic value the dilapidated properties of the H&M; and (3) if—and this is very important—the Pennsylvania Railroad makes it possible for the Port Authority, as a public agency, to continue to utilize the tracks of the Pennsylvania Railroad under the terms of the present agreement for the joint operations of the two railroads between Jersey City and Newark.

"Without the full cooperation of the Pennsylvania Railroad in agreeing in the public interest to the continued use by the H&M of the tracks of the Pennsylvania Railroad, under their existing agreements with the H&M, these plans for the reconstruction and public operation of the H&M cannot be accomplished. So, too, the project depends upon the ability of the Port Authority to acquire the bankrupt properties of the H&M on fair and realistic terms. Both of these railroad companies have been very active in their efforts to either divest themselves of their commuter operations or to obtain public financial support for their continuance. We trust, therefore, that they will be anxious to cooperate in making it possible for the two States to rehabilitate and continue the H&M services.

"If, then, it becomes possible for the Port Authority to acquire, rehabilitate and operate the H&M, we

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would propose to undertake a major rehabilitation program immediately which could be completed within approximately three years after the time that the Port Authority acquired title to the H&M properties.

"Our studies indicate that approximately $30,000,000 will be necessary to improve the physical plant of the railroad, an additional $24,000,000 to purchase new cars and $9,000,000 to rehabilitate the Hudson Terminal buildings in lower Manhattan, making a total of $63,000,000.

"The railroad's physical plant, as I have noted, over a long period of time has been permitted to deteriorate very badly. I might say that this plant deterioration has reached the point where major interruptions of H&M service occur and may be expected to increase.

"The Port Authority's $30,000,000 program for rehabilitation of the physical plant would include the immediate and necessary replacement of the railroad's obsolete signal system with a modern installation that would permit not only a greater number of trains, but safer and more reliable operation.

"It would provide an entirely new, modern power distribution system which would eliminate the frequent and time-consuming delays now experienced by H&M commuters as a result of power failures.

"It would include major rehabilitation and refurbishing of the H&M passenger stations.

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"The modernization job would also include extensive track maintenance work which would assure a smoother and more pleasant ride.

"Substantial improvements to the present car storage yards and maintenance shops as well as the provision of an entirely new storage yard and maintenance facilities to handle the additional rolling stock would be necessary.

"From time to time, and as recently as last September, the H&M has been forced to close down because of the inability of the inadequate and obsolete drainage system to function properly during serious flooding conditions. This situation would be corrected by the replacement or rehabilitation of all drainage pumps and water discharge lines in the tunnels.

"The Port Authority staff's inspection and study as well as the study and conclusions of our engineering consultants indicate conclusively that H&M's entire fleet of old cars should have been scrapped some time ago. It must be completely replaced. No less than 110 of these cars are over 50 years old and all of this old fleet has been in service for more than 32 years.

"We would purchase 186 of the most modern rapid transit cars available to replace the H&M's antiquated cars. They would be airconditioned, well-lighted, have attractive interior design and afford the best qualities in passenger comfort."

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"In addition to the replacement of this obsolete equipment, 102 new cars would have to be provided for the increased traffic which would be, and we believe could be, handled by the 'new' H&M system. This increase in traffic would result from the consummation of Commissioner Palmer's plan to bring Jersey Central passengers into Pennsylvania Station, Newark, where they would have a direct and convenient transfer across the platform to the H&M. The new H&M cars would also be needed for additional service between Hoboken and lower Manhattan if and when the Erie-Lackawanna ferry service were abandoned.

"Under the existing operating agreements with the H&M, the Pennsylvania Railroad would provide 51 of this total of 288 new cars to handle their share of passenger responsibilities to and from Newark. All of the remaining 237 new cars would be provided by the Port Authority at a cost of about $24,000,000.

"Again, if the Legislatures make it possible for us to finance this H&M project, all of these 288 modern rapid transit cars, with the cooperation of the Pennsylvania Railroad, could be rolling within a three-year period.

"With this $63,000,000 expenditure to rebuild and rehabilitate the Hudson and Manhattan for our generation and for the future, we will have brought into being, in accordance with Commissioner Palmer's plans, a modern and dependable rail connection with Manhattan for the 53,000 daily New Jersey commuters, as compared to the present volume of 35,000

commuters, who would transfer to the H&M from the Jersey Central, Pennsylvania and Erie-Lackawanna Railroads or utilize only the H&M service from Essex and Hudson Counties.

"The costs and other burdens of commuter service on these privately owned railroads will have been substantially reduced as a result of Commissioner Palmer's proposals for service improvements and modifications. These savings to the commuter railroads should in turn reduce the future cost for New Jersey taxpayers of service contracts with the State's principal rail carriers.

"I might note also that practically everything of basic importance that was sought to be accomplished in the plan proposed in 1958 by the Metropolitan Rapid Transit Commission for a five hundred million dollar bi-State transit loop connecting up the principal New Jersey commuter railroads, is met by this proposal for the reconstruction and extension of service on the H&M, and *it can be accomplished without State or municipal subsidy.*

"Travel times for commuters and other riders on the Jersey Central, Pennsylvania and Erie-Lackawanna will be at least as good as, and in many cases better than, those they experience today. In addition, passengers using the modernized H&M will be assured frequent, reliable and comfortable service.

"Insofar as northern New Jersey and particularly the City of Newark are concerned, Commissioner Palmer's plan for bringing Jersey Central passen-

gers into Pennsylvania Station, Newark, will provide a new, direct and fast rail transit connection, never available before, between the residential areas of western Union County, Somerset County and Hunterdon County and the center of Newark. Thus the plan, together with the reconstructed H&M, will make Newark the focal point of a vastly improved and expanded commuter transit service.

"There is, of course, no possibility whatsoever that either the Port Authority or any one else could operate the H&M on a self-supporting basis. The bankrupt H&M has not paid a dividend since 1932; it has not been able to meet the interest on its bonded indebtedness and has been in receivership since 1954. This is not intended to reflect upon the past management of the railroad, since its inability to earn even the interest on its bonded indebtedness is paralleled by many transit systems all over the country.

"On September 26, 1960, the day before our Executive Director advised this Commission that the Port Authority would consider acquisition of the H&M, the market value of the railroad and its properties as appraised by the price of its outstanding securities was a little more than $13,000,000. I might note that the speculative value of these H&M bonds has shown an increase of over 50% in the four months since that announcement, to a total market value of about $20,000,000 today. This speculation obviously has taken place on the basis of our indication that the Port Authority might be willing to pay approximately that sum to acquire the H&M.

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"After this study of the whole situation with all of its variables and contingencies, the Commissioners of the Port Authority are assuming that the acquisition, rehabilitation and operation of the H&M will involve an annual deficit to the Authority of about $5,000,000.

"I should add that this anticipated deficit assumes that every possible effort would be made to maintain the present fare structure.

"With the pooling of Port Authority revenues through our General Reserve Fund (which reflects the policy of the two States with respect to the future development of the public terminal and transportation facilities of the bi-State Port), we are of the opinion that an annual deficit of this magnitude can be carried by our other facilities.

"On this estimate of the H&M losses, and if we are able to satisfy prospective investors by statutory assurances that this proposal will not involve the Authority's General Reserve Fund in any other or further commuter deficit operations, we believe we can conscientiously certify, as we must under our indentures, that this financing will not impair the Port Authority's credit. On the other hand, if we are not in a position to cite such statutory assurances to those from whom we will have to borrow the money, and therefore, we are not in a position to make such a certification, we obviously would not be in a position to borrow money for the acquisition, let alone the improvement, of the H&M. Indeed, any attempt to direct the Port Authority to acquire and

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operate the H&M without such statutory assurances would so damage Port Authority credit as to put it beyond our ability to borrow money for any other Port Authority project.

"I am sure that the members of this Commission appreciate that neither the Commissioners of the Port Authority nor anyone else can divert the existing Port Authority revenues to any new project or facility, or use them, except in strict accordance with the specific provisions of our outstanding contractual agreements with investors. These explicit statutory and contractual controls require that all Port Authority revenues must first be used to meet the operating and maintenance costs of the facilities which produce them. The net operating revenues must then be applied to the principal and interest payments on the specific bonds for which they have been pledged; then all of the remaining balance must be paid into specified reserve funds.

"The monies in these reserve funds are legally available only to fulfill contractual commitments to holders of bonds secured by a pledge of reserves. The General Reserve Fund may not be pledged in support of bonds to finance a new facility under circumstances where the pledge would materially impair the Authority's sound credit standing.

"All Port Authority revenues not applied to operation and maintenance and debt service *must* be paid into one or another of these reserve funds. There are no excess revenues which are free from this contractual commitment to bondholders.

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"The most important pledges that the Port Authority has made to its bondholders are those relating to the issuance of bonds for new projects. These pledges were necessary since otherwise the security could be diluted, not only through the raiding of revenues and reserves, but just as disastrously by the unlimited issuance of bonds which have such revenues and reserves as their primary source of repayment.

"It is because of this that the Port Authority had to covenant with its bondholders not to issue Consolidated Bonds supported by the General Reserve Fund for any new facility unless it can be demonstrated that, including the new facility, net revenues will be sufficient to cover by at least 1.3 times the maximum interest and principal payments due in any future year. Furthermore, bonds for a new facility cannot be issued with a pledge of the General Reserve Fund unless the Port Authority Commissioners certify that the issuance of the new bonds will not materially impair the sound credit standing of the Authority, the investment status of the Authority's bonds, or the ability of the Authority to fulfill its commitments and undertakings. Such protections for investors under open-end revenue bond issues are not uncommon.

"Applied to the H&M proposal, I would like to make it clear that the question of whether or not we can borrow the $83,500,000 which is required, is not simply a question of whether or not we would have to pay a higher rate of interest on these funds. We can only submit to you the unanimous view of the

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Commissioners of the Port Authority that there is no possibility whatsoever of borrowing the money at all without a statutory assurance to investors that any future Port Authority responsibilities in the field of commuter rail transport over and above the present and existing interstate Hudson and Manhattan railroad system will not involve a pledge of the Port Authority's General Reserve Fund.

"I say to you as a New Jersey Commissioner, and with all the sincerity that I can command, that there is nothing arbitrary or doctrinaire about this conclusion. It simply represents the realities of investment financing and the Port Authority's credit. My business is investment financing and I say to you gentlemen that I could not sell a single Port Authority bond without such an assurance. If my responsibility were on the other side of the table, I would not buy a Port Authority bond that did not contain such an assurance.

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"At this point, and on a different phase of the subject, I might say that in our estimates of annual deficits of the H&M, we have included an amount equal to the real estate taxes now being paid on H&M properties in New Jersey and in New York City. We would propose that whatever statute is adopted should contain an authorization to cover this situation. This would be along the lines of the existing statutory provisions which permit the Port Authority to enter into agreements with municipalities to make payment in lieu of real estate taxes on prop-

erties acquired and owned by the Authority. Under the existing statutes these payments may be equal to the sum last paid as real estate taxes upon such property prior to its acquisition by the Port Authority. All of our existing agreements with New York and New Jersey municipalities under these statutes are in that maximum amount.

"We have, of course, kept Governor Meyner's office advised as to the progress of these studies through his liaison officer with the Port Authority, Commissioner Palmer. So too, Governor Rockefeller's office has been kept informed both through his Executive Secretary, Dr. William Ronan; his counsel, Mr. Robert MacCrate, and the Director of the Office of Transportation, Mr. Arne Wiprud.

"If and when the statutory authorization permitting the Port Authority to go forward with this program is adopted by the New Jersey and New York Legislatures and signed by the Governors, we are prepared to initiate negotiations with the reorganized Hudson and Manhattan company looking toward a final determination of the purchase price of the facility.

"Following the adoption of such authorization, we would also undertake formal discussions with the Pennsylvania Railroad for the continuance of existing agreements between the Pennsylvania and H&M on the joint operations of the two rairoads to and from Newark. We assume that the Pennsylvania will be willing to continue these agreements with the Port Authority, a public agency of the two States, on the

same terms and arrangements as they now have with the privately owned H&M.

"In the normal course of events, we would hope that the Port Authority might be able to acquire and commence the operation and rehabilitation program of the H&M before the end of 1961."

By Senator Farley:

"Q. Mr. Kellogg, I notice in the latter part of your statement, you said you must be given assurance by the Legislature that if they directed the Port to proceed to purchase this property, they must make a pledge to the bondholders there be no further projects involving rail. Now I appreciate that if the Legislature directs you to enter into a contract involving the issuance of bonds, there will be no impairment of obligations of contract, but I must call to your attention and the members of your Commission that one Legislature cannot bind a subsequent Legislature involving policy. If, perchance, may I illustrate—ten, fifteen, twenty years from now the respective legislatures of New York and New Jersey importune your Port Authority Commission to do something in addition involving public service, one legislature cannot bind another involving policy. Do you follow me? A. I do.

"Q. I appreciate the legal end of it involving obligation of contract, but in your statement that you be given assurance that no further services should be required of you involving rail forever hereafter—and how this legislature could bind a subsequent leg-

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islature I do not know. A. We'd have to say that to the bondholders, the ones that were going to purchase the new bonds that we as Commissioners believe that this would not endanger the 1.3 ratio.

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BY SENATOR COWGILL:

"Q. I want to clear one thing up. I got a little confused there for a minute on that policy business—in the event that the H and M were acquired on the basis of statutes passed by New Jersey and New York, they would not be called upon, that is, the Port Authority would not be called upon, to go into any further commuter problems of other roads. If bonds were issued under such legislation, you would not be able to issue any further bonds for anything else unless you were willing to certify that it would not— A. That's correct. It wouldn't say that the bonds couldnt be issued with a state guarantee later on for something else or something of that type, freight or anything else.

"Q. It seems to me on that basis, that you enter a contract on the basis of legislation passed, that contract is going to stand and some later legislature is not going to be able to change it. A. That's right.

SENATOR FARLEY:

"My question, Senator, was—and I appreciate we cannot impair obligations: In effect, would any commitment with the present legislature estop or attempt to estop any legislation involving public needs in the future?" [No answer was given at this point].

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7. This point was repeated during a colloquy between Senator Farley and Commissioner Clancy on Jan. 27, 1961:

SENATOR FARLEY:

"I say to you as a commissioner representing New Jersey we too have a responsibility of making sure that this is done throughly, intelligently and in a way that would be feasible and practical. It was testified today by Mr. Kellogg that the Port should not be bound by any other demand from the State Legislature relative to rail service. I pointed out to him—and may I say to you as a lawyer—we well appreciate that any direction we give you by enacting legislation, we could not impair any obligation such as contracts of bond issues. Likewise, you as a lawyer know that one legislature cannot bind the other involving policy five, ten, or twenty years hence.
A. I appreciate that.

"Q. So that when this Committee makes its report, we are not exonerating the Port from any responsibility for any demand for future public service by either the New York or New Jersey legislature. I want you to appreciate that fact.
A. I appreciate that fully and I am aware of the fact if a situation such as that would arise in the future, that would be a matter that we would have to discuss on its own merits with a future Governor and future legislature.

"Q. That's right.

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MR. TOBIN:

"May I say something?

SENATOR FARLEY:

"I want to call you, Mr. Tobin, relative to this situation. If you want to interject something at this time, we will be very happy to have you do so.

MR. TOBIN:

"You might want to know that this legislative assurance, as Commissioner Kellogg pointed out, would only apply to future commuter operations and only limits the use of the pledge of the general reserve fund. It only limits the pledge of the general reserve fund, nothing else. It would not typically bar Port Authority participation where some other scheme of guarantee of the bonds or something like that—

SENATOR FARLEY:

"That would have to depend on its own merit or demerit and then be considered. But I call to your attention as a Commissioner the problem of the Legislature.

MR. CLANCY:

"I am aware of the problem, but, of course, the action that is taken now with reference to the Hudson and Manhattan would not necessarily of itself bar future participation in the problem generally. It would, however, not be possible if that future participation involved any impairment of this reserve fund.

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8. At the [Farley Committee hearings], Austin Tobin, Executive Director of the Port Authority, testified in part as follows: • • •

"Q. Mr. Tobin, if my recollection is correct, speaking of the Hudson and Manhattan proposal—is my recollection correct that you were quoted whether accurately or not in the newspapers in '59 and '60 that the Port of New York Authority should not involve itself in the rail commuter problem and further that it should not undertake a deficit operation? A. Well, Senator, those statements had to do with the proposal that the Port Authority be directed to take over the whole commuter rail transit problem, which from any standpoint that we could envision it was legally and financially and every other way completely impossible. They did not have to do with this new idea developed between Commission Palmer's office and our office that this might be possible if some sort of an assurance—that we might be able to sell what we are talking about, like one hundred million dollars worth of bonds for commuter service if the bond buyers could be given some assurance as to where they were going and what the limits of their involvement were.

"Q. Would you say, Mr. Tobin, that this proposal, as suggested by you at the original meeting of this Committee, is a departure from the original attitude of the Port Authority with respect to the rail commuter problem? A. I think that certainly the idea

of being able to go into the problem to some extent, provided the bondholder on the other side could be given some assurances, certainly is a new concept.

"Q. Would you tell me what prompted the Port Authority to, shall I say, change its attitude in this respect? A. Well, I can't—

"Q. Or perhaps you have already answered that.

A. I think I have, Senator. I can't emphasize how earnestly—I know, I've lived through it through the years. The Port Authority has studied and studied and studied and worked on the possibilities of what it could do or could not do in commuter rapid transit service and has always come up against that concrete wall of the impossibility of selling bonds in the deficit commuter railroad field.

"And you will recall that a couple of years ago we did work out an involvement, if you will, in the commuter rapid transit field in New York under which New York, in the first phase of the program, is advancing $20 million with which we are buying railroad equipment, really as the agent of the State of New York. And then it has a second phase which just was passed in the New York Legislature for the the second time yesterday and will be on the ballot in November by way of a constitutional amendment, under which the State would guarantee the Port Authority a special issue of Port Authority bonds put out for the purchase of rail equipment.

"So, as we have studied this thing through the years we have been able to evolve and develop, which we have been trying to do, new financial schemes

and devices under which it was possible for us to participate and to do what we always wanted to do and to play our part in it.

"Now since certainly in all realism the idea of a guarantee of a special issue of Port Authority bonds in New Jersey is probably quite impossible and since, with the State's financial problems, it would have been hard to think of the State advancing money to the Port Authority to initiate such a program as the State of New York did, here is another financial plan that we have diligently worked out with Commissioner Palmer's help and encouragement, and starting from his initial idea in his report of March 1960 that we simply buy and lease to the Hudson and Manhattan some eight and a half million dollars worth of cars—oddly enough that was impossible—and yet we came to you in September on the basis of conferences and studies that have been going on between the Highway Department and ourselves since February 1960, with a plan which made an $80 million participation possible where an $8½ million participation was not.

"Q. But the Port Authority now is firm in its resolution that it can handle a deficit operation.

A. If we can go to the bondholders with your approval—

"Q. With these restrictions. A.—and say, you don't have to worry beyond this point, because beyond that point they wouldn't worry."

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MR. TOBIN:

"As Commissioner Kellogg testified and Commissioner Palmer testified, we can't get along without these existing rail lines. The problem, as I see it, is to maintain and preserve them and improve them as best we can and stay away from these 'wild blue yonder' $500 and $600 million plans of new transit systems, but the New York-New Jersey area must have the continued service on these existing rail lines and can't do without them. There has been tremendous accommodation of the growth of the population by the buses, but it would just be chaos and impossible today if we tried to transfer the people that come in by rail now on the Jersey Central and the Pennsylvania and the Erie-Lackawanna and, in other areas, the Long Island and the New Haven to buses. It can't be done. It becomes an absolutely essential public service, just as real and essential as streets and water and all of the other necessities of urban life are to us. And we are all in both legislatures and in the public recognizing that this has become a public problem and the programs we have been discussing here for the last two days, both here and the references to them in New York and the references to them on the Federal level, are all recognition that this has become a public problem and people must be able to get back and forth to work. Also, none of us can ask indefinitely private companies to take these staggering losses—and they are staggering."

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9. The Farley Committee record included a letter dated February 10, 1959 from Austin J. Tobin, Executive Director of the Port Authority to the Governors of New York, New Jersey and Connecticut and the Mayor of New York City, which concluded as follows:

"The Port Authority Cannot Undertake Transit Responsibilities

"It has been suggested from time to time that the Port Authority should be the agency charged with financial responsibility for rail transit in the metropolitan area, or at least with its trans-Hudson phase. In their recent Statement to the New Jersey Assembly, the Commissioners of the Port Authority dealt with this subject at length (pages 1 to 11), and submitted in conclusion that:

(1) It is legally, financially and contractually impossible for the Port Authority to assume the railroads' increasingly heavy deficits from all or part of commuter operations, or the cost of developing a new and comprehensive interstate rail rapid transit system; and that

(2) Even if it were legally and contractually possible, very quickly the assumption of rail transit deficits by the Port Authority, the self-supporting agency of the two States, would cripple and destroy the Authority's credit. It would thereby bring to a halt the program now being carried out by the Port Authority on behalf of the two States for the continued development of their essential pub-

lic marine and inland terminal facilities, airports and interstate arterial systems.

"Within the framework adopted by the two States in the Port Treaty of 1921, the Port Authority has developed a system of essential public transportation and terminal facilities in the bi-state New York-New Jersey Port District. The projects which make up this system have all been planned, constructed and operated within the completely self-supporting requirement of the two States, and without recourse to any funds derived from the taxing power or the credit of either State or any of its political subdivisions.

"Under this program six interstate bridges and tunnels between New York and New Jersey, the four major metropolitan airports and a heliport, four inland terminals (for buses, truck and railroad freight) and a $125 million system of modern docks and piers on both the New York and New Jersey sides of the harbor have all been provided and function as essential elements in the public transportation and terminal system of the region.

"Under present contractual commitments, the Port Authority will, during the next five years, build other essential facilities and additions to existing facilities including the second level of the George Washington Bridge and the Washington Heights Bus Passenger Facility, the Narrows Bridge, the Brooklyn-Port Authority Piers, the Elizabeth-Port Authority Piers, the completion of New York International Airport, and the complete modernization of

LaGuardia Airport. This program, which will require the Authority to borrow over $700 million of capital funds in the next five years, is based on express authorizations of the Legislatures and Governors of both New York and New Jersey. All these projects and facilities, like the facilities already in operation, will be self-supporting and can be financed only on such a basis. It has been overwhelmingly demonstrated that rail transit is not and can never be in this category.

"The Port Authority has, therefore, been obliged to state unequivocally that it cannot assume any financial responsibility for rail passenger transportation in the Port District. We have also noted that, even if it were legally and contractually possible, the assumption of the large and ever-increasing deficits of rail commutation would quickly destroy the Port Authority's credit and bring to a halt the entire present and future program of port and regional development which it is carrying forward on behalf of the two States. It is an ironic fact that the assumption of rail passenger deficits would not only destroy the Authority's vital programs of self-supporting transportation and terminal facilities, but would also destroy the Port Authority's ability to finance rail transit itself.

"Port Authority Assistance in Solving the Problem

"Even though it is thus impossible for the Port Authority to participate financially in any degree to the solution of the rail commutation problem, the Authority, for many years, has assisted in the study

of the problem and in the search for a solution. We stand ready today, as always, to assist in any way possible in the search for solutions to the mass transit problem in either its trans-Hudson aspect or in its over-all relation to the region as a whole."

10. In testimony before the Farley Committee on May 5, 1961 Mr. Tobin testified:

"SENATOR FARLEY: What is your plan involving the Hudson and Manhattan?

"MR. TOBIN: In the general plan that has been discussed with the legislatures and is the subject of discussion with both legislatures now, the Port Authority would propose to purchase the Hudson and Manhattan and to completely reconstruct and rehabilitate it. It would cost in excess, we estimate, of $80,000,000 to $85,000,000 to do that. It would require some 280 new cars. The plans are closely integrated with those of Commissioner Palmer for the general New Jersey commuter program. It requires a completely new signalling system and the construction also of certain new car facilities. We would plan in connection with it to pay full taxes now being paid in both states on the Hudson and Manhattan properties. We would take over as part of it the Hudson Terminal Buildings, not so much for their revenue aspects because even after you reconstruct them, they wouldn't appear to do much more than break even. But that banjo terminal of the Hudson and Manhattan is constructed inside those terminal buildings and their electrical power sub-stations, some of them, are in there and it's really

a simpler operation to take over the buildings than to try to separate the pepper and the salt as between who owns the first floor and the second floor and work that all out.

"This would require identical legislation in both states which, of course, is under active discussion. It would also require—we have advised the legislatures—some form of limitation to bondholders. In other words, nobody in their right mind would buy a Port Authority bond at the time that the Port Authority is going into the commuter rapid transit system with set and established losses that outside of the city subway system today amount to about $30,000,000 a year. Now nobody is going to buy that kind of an open-end revenue bond. But we believe that we can peddle a Port Authority commuter railroad bond if you permit us to go to the fellows who buy the bonds and say 'We are going to do this job and we can't argue with you the job won't lose money, but the Legislature has assured you that we won't go in it beyond some point, which under the discussions about the bill which was introduced in the Assembly in New Jersey was that the Legislature would agree with our bondholders that it's an odd way to express financing, but that we wouldn't commit ourselves to projects that we thought would lose in total more than 10 per cent of the general reserve fund.' Now the general reserve fund is $70,000,000 and it should be in about two or three years at about $100,000,000. It has to be 10 per cent of the outstanding bonds and there are close to $700,000,000 bonds outstanding now and there will be

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$1,000,000,000 in Port bonds outstanding in a couple of years. So 10 per cent would be $10,000,000. In other words, we would be able to say to the vice president of a trust company about to buy a Port Authority bond, 'Don't be afraid of this. It is a losing project, but the Legislature assures you that they won't ask us to go in it beyond a point where we are losing more than'—if there's $100,000,000 in bonds out—'$10,000,000.'

"Now, on the Hudson and Manhattan, I estimate we will lose $5,000,000 a year.

"SENATOR FARLEY: . . . Under the general bonding procedures that you follow, why do you make the point that it would be difficult to sell bonds by having to tell the purchasers that this would be a loss operation when you have been able to sell bonds before for loss operations and when you sell them as a general bond and not as a specific bond for the H & M?

"MR. TOBIN: Well, we have never gone into any field before where we couldn't look a bondholder in the face and say, 'W honestly believe that we can make this self-supporting and that you'll get your money back.' We have been wrong. In the case of the motor truck terminals, certainly we were wrong. And those terminals by themselves have not earned enough and without the pooling of the general reserves wouldn't be enough. But here is a point where you enter a field where no one seriously argues that you can do anything with commuter rapid transit with its 20 hour a week service but lose money and lose money big.

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"They know also that the commuter railroads around New York and New Jersey now are losing currently $30,000,000 a year and those are pretty nearly correct figures—they are not ICC formula figures. Now, as you move into that field, the whole market can panic on you and you are selling in a highly competitive securities market where the trust officer for the bank—all of this money in these large amounts are in charge of fellows carrying the responsibility of investing other people's money—he doesn't have to buy this morning a Port Authority bond; he has three or four bonds put in front of him that are of equal or better rating and that are just as fine a yield and in just the same general category if he is diversifying his portfolio. Senator, he isn't going to bother arguing with me as to whether or not we will be able to pull through in this field of commuter transit deficits—he isn't going to be able to argue with me that he needn't worry that in the future the legislatures would never ask the Port Authority to take on any more commuter deficits. In this competitive field, he isn't going to bother—he doesn't have to bother. And that's the reality of the situation.

"I know and I have reason to believe that some of the Senators sitting here know of a very large investor of Port Authority bonds who has already put them on the market because of this type of discussion and it's not an isolated case. So the credit situation that we face as we move into this new deficit field in which the City of New York typically on its subways loses $125,000,000 a year alone—as

we move in, no one is going to lend you money for 30 years without some statutory assurance of just how far we're going."

11. The following is an excerpt from the report dated June 28, 1963 of the Farley Committee:

"Peat, Marwick, Mitchell & Co., the accounting firm which made the audit of the records of the Port of New York Authority for the Committee, has submitted to the Committee its written report together with supplemental oral information.

"The basic framework and philosophy of the Port Authority with respect to its financing policies and its adherence to the principle of administering self-supporting facilities are soundly conceived. For example, the auditors reminded us that the General Reserve Fund and the pooling of revenues are the means selected by the States' Legislatures to enable the Authority:

'To finance its operations as a single enterprise rather than having to finance each of its facilities separately relying solely on the merits of that facility alone. The general reserve makes it possible for the Authority to finance new facilities which otherwise could not be financed without resorting to either state or other outside assistance in the form of advances, subsidies, guarantees or the like.'

"And after reviewing the Authority's financial structure the auditors concluded 'that few of its facilities would have been financially feasible without the ability to pool revenues of all facilities.'

"The auditors also stress that the single enterprise financial structure of the Authority has an important bearing on the Authority's accounting procedures. The auditors report that:

'The Authority's financial structure is based on a single enterprise, pooling of revenues concept. Individual facilities are not financed independent of the rest of the Authority. The facilities contribute their revenues for debt service according to their earning power without regard to the amount of bonds which were issued for their construction. For these reasons any presentation of net revenues after debt service for individual facilities is not based on actual fact. As pointed out by the Authority in submitting its report, such a presentation can only be based on arbitrary assumptions.'

"COMMUTER RAPID TRANSIT

"On September 27, 1960, at the first public hearing of this Committee, pursuant to Resolution No. 7, The Port of New York Authority announced that it would undertake an immediate study of the feasibility of that agency acquiring, modernizing and operating the Hudson and Manhattan Railroad. This was the first public expression by the Port Authority of its willingness to share in the responsibility of meeting the commuter rapid transit requirements in the area of northern New Jersey.

"At the September 27 hearing, the Port Authority suggested that:

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'The Port Authority might be able to sell bonds for the acquisition and modernization of the Hudson & Manhattan Railroad and continue the financing of the States' vital port development program:

'(a) if investors could be given contractual assurance, with statutory protection, that the Port Authority's responsibilities in the field of commuter rail transit would be confined to the present and existing interstate Hudson & Manhattan Railroad systems;

'(b) if all the Hudson & Manhattan Railroad system, including the Hudson Terminal properties could be acquired on the basis of their present realistic market values;

'(c) if the operating agreements between the Hudson & Manhattan and the Pennsylvania Railroad could be transferred to the Port Authority on reasonable financial terms, permitting the continued use by Hudson & Manhattan trains of the Pennsylvania Railroad's tracks, stations and other facilities between Jersey City and Newark;

'(d) if Commisioner Palmer's recommendation of linking the Jersey Central Railroad via the Lehigh Valley tracks with the mainline of the Pennsylvania Railroad would be carried out, thus making it possible for Jersey Central commuters to transfer at Newark, either to the Hudson & Manhattan service to downtown

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Manhattan or the Pennsylvania's uptown service to Penn Station in New York; Commissioner Palmer's plan also envisaged the eventual handling by the Hudson & Manhattan of all interstate commuters from the Erie and Lackawanna Railroads now coming into the rail terminal at Hoboken, many of whom presently use the railroad ferry to Manhattan.'

"In concluding his statement on the prospects of acquiring the Hudson & Manhattan Railroad the Executive Director of the Port Authority, Mr. Austin J. Tobin stated that:

'The Commissioners have asked me to assure you, Mr. Chairman and the members of this Committee, that the Port Authority will continue to pursue this matter to the end that we may make a report and recommendations to the Governors and to the Legislatures of New Jersey and New York. It is our hope that this may be possible before the end of this year.'

"The Port Authority's study of the Hudson and Manhattan Railroad was concluded in January, 1961. The results of that study and the Port Authority's announcement that it would be able to go forward with the Hudson & Manhattan project with appropriate authorizations were made public by this Committee's public hearing in Newark on January 27, 1961. At that hearing, James C. Kellogg, III, Vice Chairman of the Port Authority testified as to the Authority's ability to go forward with the acquisition and rehabilitation of the Hudson & Manhattan.

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"Vice-Chairman Kellogg and Mr. Tobin were questioned at length by members of this Committee on all aspects of its proposed program to acquire the bankrupt railroad. In addition the Committee heard testimony on this date and the preceding day from commuter groups, railroad representatives, individuals and civic associations on various aspects of the prospective transit responsibility of the Port Authority. These hearings, which were devoted exclusively to the subject of commuter rapid transit, resulted in a conviction on the part of this Committee that the Port Authority's proposed program to acquire and improve the Hudson & Manhattan equipment and facilities was sound and in the best interests of the people of this State.

"During 1961, the New York State Legislature enacted legislation which empowered the Port Authority to proceed with the acquisition, modernization and operation of the Hudson & Manhattan Railroad and coupled in the same bill an authorization for the Authority to undertake the development of a World Trade Center on the east side of lower Manhattan. The bill contained no statutory covenant to protect Port Authority credit against future transit responsibilities which would divert its railroad deficits to revenues and reserves pledged to its bondholders. This legislation proved unacceptable to New Jersey because of the manner in which these two projects were 'packaged' in one statute and because the absence of such a statutory covenant, in our judgment, endangered the future utility of the Port Authority to the 2 States. Accordingly, an

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impasse developed in 1961 between the States of New York and New Jersey on the appropriate form of legislation for these two projects.

"This Committee was convinced that the credit problem which had been pointed out by the Port of New York Authority was a valid and real one and that the Port Authority could not assume responsibility for the complete burden of the deficit-ridden commuter railroad problem in the area of northern New Jersey and New York. If the Port Authority were to receive such unrestricted responsibility, there is no question but that its sound credit position would be seriously impaired, if not destroyed, and it would become impossible for the Authority to continue to move forward either with such a rail program or with other vital transportation and terminal facilities and other facilities of commerce desired by the 2 States in continuing the Port Authority's tradition as a public agency.

"As a result of lengthy discussions and firm insistence by the New Jersey Division of Railroad Transportation that Port Authority operation of the Hudson & Manhattan Railroad must extend beyond the main stem, which was concurred in by New York State conferences, the following program was adopted as acceptable to the States of New York and New Jersey:

1. Extending the Port Authority's authorization beyond the present Hudson & Manhattan Railroad system;

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2. Limiting the authorization at this time to extensions of that system within a delineated area to permit over-the-platform transfer of passengers between the Hudson & Manhattan Railroad and the major passenger railroads operating in New Jersey;

3. Limiting by a constitutionally-protected statutory covenant with Port Authority bondholders the extent to which the Port Authority revenues and reserves pledged to such bondholders can in the future be applied to the deficits of possible future Port Authority passenger railroad facilities beyond the original Hudson & Manhattan Railroad system;

4. Measuring that limit by 10% of the amounts of the Port Authority's General Reserve Fund at the time (or 1% of its equity, if larger, in that Fund and in its bridges and tunnels and other facilities owned and operated by it) so that a new deficit ridden passenger railroad facility can be added to the Port Authority's General Reserve Fund family of facilities (and thus be able to syphon off the pledged revenues of the self-supporting facilities and the pledged reserves accumulated therefrom) only if the estimated annual deficit of all Port Authority passenger railroad facilities, including the proposed new one, do not exceed the limiting figure at the time; and

5. Permitting enlargement beyond the limiting figure only to the extent of state guarantees of

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Port Authority deficit from passenger railroad facilities.

"Late in 1961, a proposal was made to shift the location of the proposed World Trade Center to the west side of Manhattan and to integrate it physically with and directly above the lower Manhattan terminal of the Hudson & Manhattan Railroad. This program had appeal for the State of New Jersey and, in effect, meant that the Port Authority's improvement of the Hudson & Manhattan system, including its extensions, and the World Trade Center were, in fact, one integrated project. By this time, general agreement among the officials of both the States of New York and New Jersey had also been reached on the extent of the use of the Port Authority's revenues and reserves in meeting transit deficits. Thus, the way had generally been cleared for prompt legislative action by both States authorizing the Port Authority to proceed as rapidly as practicable with the single project—the World Trade Center and the Hudson Tubes and its extensions.

"It was with a great deal of satisfaction that the full membership of this Committee sponsored the legislation authorizing the Port Authority to proceed with this project, one of the most important statutes ever to be enacted by the New Jersey State Legislature. On February 13, 1962, both Houses of the Legislature passed this bill by unanimous votes (with one abstention in each House) and Governor Hughes signed the Bill on the same day.

Soon thereafter New York enacted the same Legislation.

"By virtue of its thorough investigation of all aspects of the Port Authority's operations, and its work with the Port Authority and with the public officials of both States this Committee was enabled to evaluate and to participate in bringing about a Port Development project which, in our opinion, will be of inestimable value to the citizens of the State of New Jersey and the Metropolitan area.

"Our Committee has been impressed with the performance and untiring efforts of the Port Authority Commissioners both of New Jersey and New York toward insuring the maintenance and growth of our great Port. The efficiency of the Executive Director, Austin J. Tobin, and members of his staff has made possible our thorough, frank and productive research of an Agency which in its record of performance is excellent.

"CONCLUSIONS

"The Committee has discharged its assignment under Senate Resolution No. 7. In connection with the first branch of that resolution, we have studied the entire financial structure and operations of the Port Authority, including the receipts and disbursements of its funds. We find the structure appropriate to the assignments which the State Legislatures have made to the Port Authority and soundly devised to achieve the lowest possible cost for borrowed money. We are conscious that the Port

Authority, having no taxing power, can operate only by continuing the cycle of borrowing money to provide facilities which yield revenues which repay the borrowings and establish the reserves to permit additional borrowings. We are mindful that in the original Compact of 1921 the 2 States recited that the cooperation of the States was required 'in the encouragement of the investment of capital.' The Authority has in our judgment balanced the public necessities against the needs to attract private capital which can only be attracted by a sound credit and confidence in efficient management.

"In studying the receipts and disbursements of funds we were led to consider the entire internal organization of the Port Authority and its control to achieve efficiency and economy. We retained outside professional auditors to make a complete and disinterested audit of the Port Authority. On the basis of their report we have concluded that the Port Authority employs good business techniques and follows sound and prudent management polices and practices to the end that the public is best served, and that the policies employed by the Port Authority operate to minimize its construction and operating costs, to develop fully its revenues other than bridge and tunnel tolls and to avoid favoritism in any of its business transactions. The internal policies of the Authority are soundly conceived, clearly contained in written instructions and complied with by the Port Authority staff. The auditors studied the particular sensitive areas of purchasing contracts and concession letting, the rental

of space, the procurement of insurance, the acquisition of real property and related fields. On the basis of their report we are satisfied that the Port Authority's techniques are soundly conceived and efficiently followed.

"Initially we assumed that it was possible to achieve detailed reporting of net operating results facility by facility not only after operating expenses but after debt service as well. The auditors' report has explained why this is not possible without arbitrary assumptions. We therefore conclude that the Port Authority has performed its duty to report properly on the financial results of its operations when it combines the debt service of facilities which have been soundly combined for financing purposes. We have considered the question of the size of the Port Authority from the point of view of its assets and revenues. We find that the size of the Port Authority is commensurate with its responsibilities vested by the Legislatures and with the growth and progress of the Northern New Jersey—New York metropolitan area which it serves.

"Also with regard to the first branch of the Senate Resolution No. 7, the Commission has studied the use and distribution of the surplus revenues of the Port Authority to determine how they may best 'inure to the benefit of the citizens of this State.' We conclude that the best use of such surplus revenues is to provide the credit base which will permit the financing and effectuation of such additional facilities as the two State Legislatures wish from time to time to achieve without taxation and through

the instrumentality of the Port Authority. The General Reserve Fund Statutes of 1931 established that policy and unquestionably the policies should be continued. The concept of the Port Authority articulated by the Investigating Committee of 1940 reflected that approach and that legislative judgment was vindicated by the record of growth and achievement of the Port Authority over the past two decades. We are in accord with these findings.

"With regard to the third branch of our authorizing resolution, we have studied the responsibility and accountability of the Port Authority to the Legislature of this State and to its citizens. We have established that the Port Authority is accountable to this Legislature and that accountability was evidenced by the complete responsiveness of the Port Authority to all of the requirements of this Committee in pursuing its investigation. It is recommended, however, that the Port Authority furnish to the Legislatures the Minutes reflecting their activities at the same time they are furnished to the Governors of the respective States.

"As required in the Compact, the Port Authority annually submits a report to the Legislatures setting forth in detail the operations and transactions conducted by it. Upon receipt of this report we urge that the Legislature, through its regularly established committees, annually invite officials of the Authority to appear before them to answer questions and to provide any further information on the operations and activities of the Authority. We believe such a regular and personal report and examination would expedite the work of the Legislature, and also would provide the public with useful

information regarding the Authority and would emphasize the continuous responsibility and accountability of the Port Authority to the respective Legislatures.

"With regard to the responsibility and accountability of the Port Authority to the citizens of New Jersey, it is clear that this responsibility and accountability must continue to be through the Governors and Legislatures of the two States.

"The Port Authority has attempted to keep the Governors advised as to such of its proposals as it deems controversial before they are adopted so as to obtain the benefit of the thinking of the respective Governors' viewpoints and avoid the necessity of veto and modification to meet the Governors' objections. The veto of the Governor continues as a most effective instrument for assuring that the policy of the Port Authority cannot depart from the policy of either State. We observe that the Governors have not hesitated to use the veto power when they deemed it appropriate.

"With regard to the final item of the third branch of our authorizing resolution, we have investigated whether or not the Port Authority is fulfilling its statutory duties and obligations. We have concluded that the Port Authority has not exceeded the powers vested in it by the two States and that it has met all of its obligations and fulfilled its statutory duties. The sole exception was the commencement of the Third Tube of the Lincoln Tunnel under existing authorization to construct the facility. The Legislature subsequently amended the statutes to bring this project within the Authority's statutory duties. It

will be remembered that the initial compact and even the comprehensive plan of 1922 were mere charters of ultimate goals. The Legislatures have directed the Port Authority's course by specific statutes from year to year. By granting and withholding particular authorizations they have set the limits within which the Port has operated.

"Over the years the Port Authority has developed and grown into a full-fledged economic entity of proportion and maturity in the fulfillment of programs designed for the progress and development of the States which authored its existence. While the Authority is a great contributor to progress, and development of the States which authored its existence, at the same time it serves as a barometer portending trends and marking goals for the future. We feel that the Port Authority has been a constructive influence in the economic life of the State and so long as it maintains its traditions and standards of public service, and at the same time continues to manifest a sensitivity and responsiveness to public need and progress, it should be given official encouragement and support in its endeavors.

Respectively submitted,

By:

FRANK S. FARLEY, Chairman
WAYNE DUMONT, JR.
WILLIAM E. OZZARD
RICHARD R. STOUT
JOSEPH W. COWGILL
JOHN A. LYNCH
WILLIAM F. KELLY, JR.
DONAL C. FOX"

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12. The following is an excerpt from the 1960 Annual Report of the Port Authority:

"Hudson & Manhattan Railroad

"In September 1960, the Port Authority outlined a proposal for financing the purchase, modernization, and operation of the Hudson & Manhattan Railroad. This development was the result of a series of meetings and discussions between Dwight R. G. Palmer, New Jersey State Highway Commissioner, and the Port Authority, starting in February 1960, which sought to find a means by which the Authority could assist in the solution of the trans-Hudson rail transit problem and still carry out the essential self-supporting port development program authorized by the two States.

"The Hudson & Manhattan, which provides an essential trans-Hudson commuter service for 31 million passengers a year, began operations in 1908. It provides services between Newark, Jersey City and Hoboken in New Jersey and New York City through two branches—one to the Hudson Terminal in downtown Manhattan and the other uptown to 33rd Street and Sixth Avenue. The H&M has been in bankruptcy since 1954. Under the proposed plan of reorganization of the company which is expected to be put into effect in 1961, the railroad and real estate activities would be separated. It is doubtful whether, under this plan, the railroad could remain in operation for more than two years.

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"Port Authority Study Conducted

"Following the September announcement, the Port Authority initiated a comprehensive study to analyze all aspects of possible Port Authority acquisition, modernization and operation of the Hudson & Manhattan.

"The study was devoted to a thorough analysis of the plant and equipment presently in service, including the need for complete rehabilitation of stations, tracks, and the railroad's signal and power systems. The study revealed that such a rehabilitation for the railroad alone would cost about $30,000,000. Similar study of the need to rehabilitate and modernize the Hudson Terminal Buildings in lower Manhattan indicated that capital improvements of about $9,000,000 would be required.

"The study also revealed that all of the old fleet of H&M cars, from 32 to 52 years old, should be replaced. A total of 288 modern and air-conditioned cars would have to be purchased as replacements and to provide for the anticipated additional service required under Commissioner Palmer's plans for consolidating and re-routing of certain New Jersey commuter rail services. This would add another $24,000,000 to the rehabilitation cost of the Hudson & Manhattan.

"The capital requirements for complete rehabilitation, therefore, would amount to approximately $63,000,000, not including the cost of purchasing all of the Hudson & Manhattan properties. The Port Authority pointed out to a New Jersey Senate Com-

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mission that in the bankruptcy proceedings of the Hudson & Manhattan Railroad Company the court had approved an SEC finding that the price which might be realized upon a sale to a private corporation of H&M properties, including the Hudson Terminal Buildings, would not be more than $20,500,000. Thus, the total capital cost of such an acquisition and modernization program should approximate $83,500,000 and would assure safe, comfortable, reliable trans-Hudson commuter service for our generation and the future.

"DEFICIT OPERATION

"Our studies concluded that there is no possibility that either the Port Authority or any other organization could operate the H&M on a self-supporting basis. After taking into consideration all of the variables and contingencies, our studies indicated that the acquisition, rehabilitation, and operation of the H&M by the Port Authority would involve an estimated annual deficit to the Authority of about $5,000,000—with every effort being made to maintain the present fare structure.

"STATEMENT OF THE VICE-CHAIRMAN

"Upon completion of the study, Port Authority Vice-Chairman James C. Kellogg, III, in a statement on January 27, 1961 before a New Jersey Senate Commission, presented for the consideration of the Commission and the Governors and Legislatures of New Jersey and New York, the findings of the study together with the view of the Commissioners of the

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Port Authority on the type of authorization by the two States which would permit the Port Authority to finance the acquisition, modernization, and operation of the Hudson & Manhattan Railroad.*

"In this regard, Commissioner Kellogg stated:

'With the pooling of Port Authority revenues through our General Reserve Fund (which reflects the policy of the two States with respect to the future development of the public terminal and transportation facilities of the bi-State Port), we are of the opinion that an annual deficit of this magnitude ($5,000,000) can be carried by our other facilities.

'On this estimate of the H&M's losses, and if we are able to satisfy prospective investors by statutory assurances that this proposal will not involve the Authority's General Reserve Fund in any other or further commuter deficit operations,** we believe we can conscientiously certify, as

"*The Port Authority has no present effective legislative power would would enable it to undertake the financing and effectuation of such a facility. As a bi-State agency, the Port Authority is able to proceed with undertakings only when they have been authorized under concurrent legislation passed by both the States of New Jersey and New York."

"**The State of New York on April 6, 1961, enacted legislation sponsored by Governor Rockefeller on the subject of Port Authority acquisition, improvement and operation of the Hudson Tubes and related properties and of the effectuation by the Port Authority of a World Trade Center. The New York legislation was in the form of a single act authorizing the Port Authority to effectuate these two facilities which the act describes as 'combined port development facilities' upon the terms and conditions set forth therein. This act contains no covenant with, or assurance to, Port Authority bond-

we must under our indentures, that this financing will not impair the Port Authority's credit . . .'

"The Vice-Chairman went on to testify that the Commissioners of the Port Authority might, therefore, be able to sell bonds for the acquisition and modernization of the Hudson & Manhattan Railroad and to continue the financing of the two States' vital port development program: (1) if the Legislatures of New Jersey and New York enact the legislation which would make it possible for the Port Authority to finance such a project; (2) if it is possible to acquire at a fair and realistic value the dilapidated properties of the H&M; and (3) if the Pennsylvania Railroad makes it possible for the Port Authority, as a public agency, to continue to utilize the tracks of the Pennsylvania Railroad under the terms of the present agreement for the joint operations of the two railroads between Jersey City and Newark.

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holders on the subject of future Port Authority responsibilities in the field of commuter rail transit.

"In the State of New Jersey Assembly No. 519, sponsored by the Governor, would authorize the Port Authority to acquire, improve and operate the Hudson & Manhattan Tubes and related properties, and contains a proposed covenant by the two States and with certain Port Authority bondholders purporting to limit the application of pledged Port Authority revenues and reserves for commuter railroad purposes to purposes in connection with the Hudson Tubes. This bill would permit the application of such pledged Port Authority revenues and reserves in the future for any other commuter railroad as to which certain certifications would have first been made by the Port Authority.

"In the opinion of Port Authority General Counsel and Bond Counsel, the New York act will not become effective upon the enactment of New Jersey Assembly Bill A-519 and if New Jersey Assembly Bill A-519 is enacted, such bill will not become effective without further New York legislation of like effect."

"Throughout the Hudson & Manhattan study the Port Authority worked closely with Commissioner Dwight R. G. Palmer in his capacity as head of the Division of Railroad Transportation of New Jersey. The Governor's Office in New York State and the Director of the New York State Office of Transportation, Mr. Arne C. Wiprud, were consulted as the study and proposal moved forward. In his statement before a New Jersey Senate Commission, Commissioner Palmer endorsed the findings of our study, stating that 'from my personal point of view, acquisition of the H&M is a must. All our plans hinge on it.' In addition, the New York-New Jersey Transportation Agency, of which Commissioner Palmer and Mr. Wiprud are the two official members, recommended to the Governors of New York and New Jersey that their States take immediate action to authorize the Port Authority to acquire, modernize and operate the Hudson & Manhattan Railroad. They termed this proposal 'the key to any plan for the solution of the trans-Hudson commuter problem.'" (Stip. 171-195)

13. The following is an excerpt from the 1961 Annual Report of the Port Authority:

• • •

"FINANCIAL ASSURANCES

"The proposal to assume responsibility for Hudson Tubes deficits constituted a marked departure from the policy of the two States to authorize the Port Authority to undertake only such facilities as were capable of eventual self-support. The inevitable deficits from the Hudson Tubes facility can be

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met only from the pooled revenues and reserves derived from the self-supporting facilities of the Port Authority. These revenues and reserves have all been pledged to the holders of outstanding bonds the proceeds of which have financed the public facilities now operated by the Port Authority.

"The undertaking of any additional public facilities by the Port Authority requires the ability to pledge these revenues and reserves for the new bonds which may be issued to effectuate such additional facilities. The Port Authority could not propose to dilute these revenues and reserves by the Hudson Tubes deficits and preserve its credit unless bondholders, present and prospective, could be assured that the dilution would be maintained within manageable proportions.

"After careful consideration the Board was of the opinion that the deficits anticipated for the basic Hudson Tubes system would be within the limits which prospective investors would accept without a downward revaluation of the Port Authority's credit. On the other hand the possibility of unlimited Port Authority responsibility for all Port District commuter railroad deficits far exceeded such limits.

"During 1961 various proposals were discussed with representatives of the two Governors and the legislative leaders of the two States and the Port Authority to agree on minimum financial assurances which might be included in any authorizing legislation so as to preserve the Port Authority's ability, with unimpaired credit, to continue to discharge its responsibilities to the people of the two States.

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"As the year ended, agreement was crystallizing on a formula which would limit the ability of the Port Authority to pledge or apply any of its revenues or reserves already pledged to bondholders for new bonds to finance an additional railroad facility beyond the basic Hudson Tubes system, unless the additional facility could be certified by the Port Authority Commissioners to be self-supporting or else to involve permitted deficits within certain specified limits. Generally, the limit was an amount which, when added to the deficits on prior Port Authority passenger railroad facilities including the Hudson Tubes, would produce a total not exceeding 10 per cent of the amount in the General Reserve Fund with certain adjustments. Agreement was crystallizing also that such financial assurances would take the form of a bi-state statutory covenant which would not be subject to impairment by either the Port Authority or the States.

"With agreement approaching at the end of the year on the form and content of the financial assurances, the site of the World Trade Center, and the extent of authorized Hudson Tubes extensions, there was a good prospect for early bi-state agreement on the necessary legislation to effectuate the unified World Trade Center-Hudson Tubes project.*"

"* On February 13, 1962, the New Jersey Legislature unanimously passed, and Governor Hughes signed, legislation authorizing the Port Authority, upon concurrence by New York, to go forward with the combined Hudson Tubes-World Trade Center project. This statute included covenants with bondholders along the lines described in the text. Identical legislation was finally adopted by the New York Legislature on March 7, 1962. It will require Governor Rockefeller's signature to become law."

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14. In early 1962, New York and New Jersey enacted legislation authorizing the Port Authority to construct the World Trade Center near the Hudson River and to take over the Hudson & Manhattan Railroad "as a unified project" on the basis of detailed legislative findings of the needs for this project. See N.J.S.A. §§ 32:1-35.50 *et seq.* As part of this statute (N.J.S.A. §§ 32:1-35.55), the two States enacted the following provision:

> "The 2 States covenant and agree with each other and with the holders of any affected bonds, as hereinafter defined, that so long as any of such bonds remain outstanding and unpaid and the holders thereof shall not have given their consent as provided in their contract with the port authority, (a) the 2 States will not diminish or impair the power of the port authority (or any subsidiary corporation incorporated for any of the purposes of this act) to establish, levy and collect rentals, tolls, fares, fees or other charges in connection with any facility constituting a portion of the port development project or any other facility owned or operated by the port authority of which the revenues have been or shall be pledged in whole or in part as security for such bonds (directly or indirectly, or through the medium of the general reserve fund or otherwise), or to determine the quantity, quality, frequency or nature of the service provided in connection with each such facility; and (b) neither the States nor the Port authority nor any subsidiary corporation incorporated for any of the purposes of this act will apply any of the rentals, tolls, fares, fees, charges, revenues or reserves, which have been or shall be pledged

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> in whole or in part as security for such bonds, for any railroad purposes whatsoever other than permitted purposes hereinafter set forth."

15. Governor Rockefeller's statement issued in connection with this legislation provided in part:

> "March 27, 1962
>
> "The enactment of this measure concludes an agreement between the States of New York and New Jersey which is of first-rank importance to the economic well-being and development of the New York-New Jersey metropolitan region and to the continued vitality of this region as a major center of job opportunities.
>
> "Under this legislation, which is in the form of a single bill, the Port of New York Authority is authorized to undertake a unified port development project, which will include the establishment and construction of a World Trade Center on the lower west side of Manhattan, the acquisition and rehabilitation of the Hudson Tubes, and extensions and improvements of the Hudson Tubes service.
>
> "Both components of the unified port development project are aimed at one goal, the continued economic vitality and prosperity of the bi-state metropolitan region.
>
> • • •
>
> "The salvaging of the Hudson & Manhattan Railroad and the extension and improvement of its service is of vital importance of the commuters of both States.

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• • •

"The need for this measure is apparent:

• • •

"Hudson Tubes

"Adequate commuter rail transportation is essential to prevent the economic strangulation of metropolitan New York.

"This State has a vital economic stake in the maintenance and improvement of rail commuter service between New Jersey and Manhattan.

"The Hudson and Manhattan Railroad has been, over the years, an unsuccessful operation. It has not offered the effective trans-Hudson commuter rail service that is so urgently needed.

"Under this bill the Port Authority will take over the Hudson Tubes and do the kind of job that is called for.

• • •

"This single bill unifies both components of the port development project physically by relocating the World Trade Center complex, previously planned on the east side of lower Manhattan, to an area on the west side encompassing the present H & M Railroad Terminal. The existing terminal buildings will be removed. The tracks will be realigned to increase allowable train speeds, platforms will be expanded to increase train capacities, lobby and concourse facilities will be reconstructed and new, modern terminal facilities will be provided.

• • •

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"To preserve the Port Authority's credit strength the bill includes a covenant by the two States that additional deficit financing of future railroad projects will only be undertaken within the financial limits set forth in their covenant.

"The bill authorizes the City of New York and the Port Authority to agree on the use of urban renewal powers in the effectuation of the project and provides for agreements by the Port Authority with the municipalities concerned to hold the municipalities harmless from loss of taxes on property acquired for the project.

"I take great pleasure in approving this legislation which completes the authorization for The Port of New York Authority to proceed with this great public program. It represents the bringing of many resources to bear in solving most serious problems peculiar to the great bi-state metropolitan area.

"The bill is approved.

Nelson A. Rockefeller"

16. "Affected bonds" were defined by the 1962 statute to include all bonds secured in whole or in part by the General Reserve Fund of the Port Authority. All Port Authority Consolidated Bonds issued since 1952 have been secured by the General Reserve Fund under the terms of the Consolidated Bond Resolution adopted October 9, 1952.

17. "Permitted purposes" were defined to include: "(i) the Hudson tubes as authorized and limited on the effective date of this covenant and agreement, (ii) railroad freight

transportation facilities or railroad freight terminal facilities, (iii) the construction, installation and maintenance of railroad tracks and related facilities on vehicular bridges owned by the port authority, (iv) any other railroad facility established, acquired, constructed or otherwise effectuated by the Port Authority (including but not limited to Hudson tubes extensions) as to which the port authority shall have first certified either that said other railroad facility is self-supporting as hereinafter defined or, if not, that at the end of the preceding calendar year the general reserve fund contained an amount equal to 1/10 of the par value of bonds of the port authority which were outstanding at said year end and which were legal for investment as defined in the general reserve fund statutes and that the group of facilities consisting of such other railroad facility and of all prior other railroad facilities will not produce deficits in excess of permitted deficits as hereinafter defined."

18. With respect to permitted purpose (iv), a passenger railroad facility would be deemed to be "self-supporting" if the "amount estimated by the port authority for the ensuing 10 years to be the average annual net income (computed without deduction of debt service) derived from or incidental to such facility equals or exceeds the amount estimated by the port authority for such 10 years to be the average annual debt service upon bonds for purposes in connection with such proposed facility."

19. If a passenger railroad facilty [other than the Hudson Tubes, as defined in the statute, or a facility situated upon a vehicular bridge owned by the Port Authority] was not "self-supporting," then none of the revenues or reserves of the Port Authority (no matter how substantial)

could be used for that passenger railroad facility beyond the "permitted deficits" of the facility.

20. "Permitted deficits" were defined to mean that the total estimated deficit (after including estimated debt service) for "the ensuing 10 years" as certified in writing by the Governors of the two States of the Hudson Tubes system as authorized and existing at the time of the 1962 legislation and of any additonal non "self-supporting" passenger railroad facility could not exceed one-tenth of the General Reserve Fund as of the calendar year prior to the certification.

21. On September 1, 1962, following enactment of the Hudson Tubes-World Trade Center legislation referred to above, the Port Authority, through a wholly-owned subsidiary (Port Authority Trans-Hudson Corporation), assumed ownership and operating responsibilities over the Hudson Tubes. The Commissioners' 1962 certification made with respect to the acquisition of the PATH System was made on the basis of an opinion of A. Gerdes Kuhbach, the Director of Finance of the Port Authority, which was prepared at the request of the Commissioners. (Stip. 201-209) • • •

22. The 1962 Annual Report of the Port Authority (p. 32) stated:

> "The Port Authority became a rail transit operator at 12:01 a.m. on September 1, 1962, when the Port Authority Trans-Hudson Corporation (PATH), a subsidiary of the bi-state agency, acquired title to and began operation of the Hudson

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Tubes, the former Hudson & Manhattan Railroad System.

"The assumption of responsibility for operating and rehabilitating the H&M system was the signal for the commencement of a projected $150,000,000 modernization program to change this rundown but key interstate rapid transit line into an efficient, convenient, and dependable public transportation service.

"Proposals for the acquisitions and rehabilitation of the Hudson & Manhattan were first publicly advanced by the Port Authority in September, 1960, following intensive studies of the Port District commuter rail situation over a period of many years.

"The Hudson & Manhattan, in bankruptcy since 1954 and hampered by obsolete and inadequate facilities and equipment, faced abandonment. In view of the key role which the line played in the Port District's transportation system, such abandonment could not be permitted.

"It was on this note that the Port Authority proposed late in 1960 that it should be authorized to acquire, operate and rehabilitate the H&M. At the same time, the Port Authority advised that investors in its bonds should be given adequate safeguards by the Legislatures of New Jersey and New York against the irreparable impairment of Port Authority credit which would result if there were no limit to the Port Authority's future involvement in additional deficit undertakings."

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23. Neither the 1963 nor the 1964 annual reports of the Port Authority referred to the 1962 Covenant, but subsequent reports explicitly referred to the Covenant.

24. The 1971 Annual Report of the Port Authority (page 57) stated:

> "The 1962 statutes adopted by the Legislatures of the two States, which authorized Port Authority acquisition of the interstate Hudson and Manhattan Railroad, specifically recognized and met the fundamental need of protecting the credit of the Port Authority to insure that it could continue its self-supporting programs so vital to the economy of the two States in accordance with the directives of the two Legislatures. The Legislatures recognized that the credit of the Port Authority would be impaired if the Authority undertook responsibility for the operation of such a perpetual deficit facility, unless the States entered into a contract with the Authority bondholders which gave assurance that additional deficit financing of future railroad projects would be undertaken only within specific financial limits." (Stip. 210-212) • • •

26. The 1973 Annual Report of the Port Authority (Stipulation, Exhibit III) stated:

> "The 1962 statutes adopted by the Legislatures of New York and New Jersey, which authorized Port Authority acquisition of the interstate Hudson and Manhattan Railroad, provided by way of a statutory covenant with the holders of affected bonds that deficit financing of additional passenger railroad

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facilities would be undertaken only within specific financial limits.

"Effective May 10, 1973, the two States amended the 1962 statutes to provide that this statutory covenant shall not apply to the holders of obligations issued by the Authority after such date. Thus, the covenant does not apply to the holders of $100 million Consolidated Bonds, Fortieth Series, issued by the Authority on June 20, 1973, or to the holders of $100 million Consolidated Bonds, Forty-first Series, issued by the Authority on October 9, 1973, nor does the covenant apply to the holders of the Authority's promissory notes issued in an aggregate of $100 million to fourteen banks and trust companies in connection with the December, 1973 bank loan. The last issue of Port Authority obligations to which the statutory covenant attached was $150 million Consolidated Bonds, Thirty-ninth Series, due 2007, issued by the Authority on February 9, 1972. As recommended by Governor Byrne, a bill intended to repeal the statutory covenant with respect to all outstanding bonds has been introduced in the New Jersey Legislature. This bill provides that it is to take effect upon the enactment of concurrent New Jersey-New York legislation and a similar bill has been introduced in New York. Litigation is currently pending in New Jersey and New York seeking to invalidate the existing statutory covenant. Cross motions for summary judgment have been made by plaintiffs and by defendant Port Authority in both the New Jersey and New York actions. In addition, United States Trust Company of New York is joined

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as a defendant in the New Jersey action as Trustee for the 40th and 41st Series of the Authority's Consolidated Bonds, as the holder of a significant amount of outstanding obligations of the Authority, and as a class representative on behalf of the holders of all outstanding bonds of the Authority, and has joined in the Authority's motion for summary judgment."

27. In 1973, PATH served 25.4 percent fewer passengers than in 1972 because of a nine week strike called by the Brotherhood of Railway Carmen. Following the strike settlement, PATH returned to service with 20 percent fewer riders and soon returned to a level 12 percent below 1972. It was only at the end of 1973, with the impetus of the energy crisis that PATH traffic returned to a level only 2 percent below 1972. (see Exhibit III, page 15). According to the 1973 Annual Report submitted by PATH to the Interstate Commerce Commission, the net operating deficit of PATH in 1973 was $17,322,355*. The total 1973 deficit as reported to the Interstate Commerce Commission was $22,733,475, which included interest on unfunded debt in the amount of $6,281,934, which was charged to PATH by the Port Authority to reflect an amount equivalent to the Port Authority's interest cost on the investment in PATH's road and equipment, including the terminal facilities at the World Trade Center and the Journal Square Transportation Center. The total cumulative deficit of PATH through the end of 1973, as reported to the Interstate Commerce Commission, was $125,079,735*. (Stip. 212-214) • • •

* These figures do not include general administration expenses. The Port Authority has been advised by the ICC that it will have to amend its 1973 and prior year reports to reflect, as well as include in all future reports, the cost of general administration expenses.

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In 1973, using the Port Authority's accounting procedures, the PATH deficit was $24,913,000, calculated as follows:

Gross Revenues	$ 9,426,100
Operating Expenses	27,596,100
Net Operating Deficit	18,170,000
Debt Service*	6,743,900
Deficit	$24,913,900

The main difference between the ICC figures and the above figures are: (1) the ICC figures do not include general administrative expenses of $4,274,600, whereas the Port Authority's figures do; (2) the ICC figures include depreciation of $2,556,200, whereas the Port Authority's figures do not; and (3) the ICC figures include only interest, on capital investment, of $6,281,900 whereas the Port Authority's figures include both principal and interest of $6,743,900.

PATH in fact has incurred an annual deficit after debt service for each of the last five years in excess of 10 percent of the General Reserve Fund. Accordingly, under the

* A certain amount of certain Consolidated Bond issues has, since 1962, been allocated by the Treasurer of the Port Authority to PATH. The figure in the above chart represents the debt service on the aggregate amount of such allocations, excluding such allocations attributable to construction in progress, which is capitalized until completion. Thus the debt service figure in the above chart includes allocations attributable to PATH Condemnation Payments, World Trade Center Terminal, Passenger Cars and Other Completed Rail Rapid Transit, and excludes allocations attributable to work in progress at Penn Station-Newark and on rail rapid transit and almost all of the Journal Square Transportation Center which was put in service in 1974. See Chart on p. [684a] for principal amounts invested.

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terms of subparagraph (b) of the 1962 Covenant, the Port Authority would have been precluded from applying any of its revenues or reserves to any other deficit passenger railroad operations.

28. The Port Authority referred to the existence of the 1962 Covenant in the Official Statement issued in connection with each of the Consolidated Bond financings subsequent to the enactment of the 1962 Covenant.

A preliminary Official Statement was usually distributed to the underwriting group, certain selected dealers and financial institutions approximately a week prior to the commencement of an offering. The final Official Statement was distributed to each original purchaser of Consolidated Bonds either prior to or with delivery of the Bonds or confirmations thereof. The annual report of the Port Authority is also distributed broadly. For example, 11,700 copies of the 1973 Annual Report have been distributed, including copies to all New York and New Jersey legislators, all Port District Congressmen and Senators, 750 copies to media representatives and 1,800 copies to a list of dealers in municipal bonds, registered bondholders, banks, trust companies, insurance companies and other financial institutions. Those on the latter list have specifically expressed interest in receiving the report.

29. The Port Authority has invested $185,800,000 of its own funds in PATH as of December 31, 1973. The accumulated ICC operating deficits of PATH totals $125,000,000, of which approximately 17 million constitutes depreciation. The breakdown of the $185,800,000 capital investment of the Port Authority is as follows:

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PORT AUTHORITY OF NEW YORK AND NEW JERSEY
CAPITAL INVESTMENT IN PATH
THROUGH DECEMBER 31, 1973
(In Millions of $)

Journal Square Transportation Center	$ 28.5
Condemnation Payments	54.7
PATH Terminal at W.T.C.	37.8
Passenger Cars	35.4
Other Rail Rapid Transit—completed	27.0
Penn Station Newark—in progress	.3
Rail Rapid Transit—in progress	2.1
	$185.8

(Stip. 215-218) • • •

30. Under the aegis of the Port Authority, PATH became one of the nation's most modern and efficient rapid transit systems. It was the first rail transit system in the world to be fully air-conditioned. In 1973, when PATH was shut down by a strike for two months, PATH carried more than 30,000,000 passengers with an overall on time performance of 97.2 percent. (1973 Port Authority Annual Report, page 11.) PATH carries more than 70 percent of all passengers entering New York City by rail from New Jersey. (PATH—Plainfield Information Booklet, page 2.)

31. The current levels of peak hour traffic carried from Hoboken and from Newark are the highest ever in the history of the system. Even in the late 1920's when the H&M carried nearly three times as many daily passengers, the peak hour demand at Hoboken totalled about 12,500 (vs. 16,000 today) and at Newark approximately 4,000 (vs. 7,300

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today). The costs incurred for crews and equipment are determined principally by peak hour requirements. Nearly one-half of PATH's current weekly traffic is carried in the two peak hours. The basic PATH interstate fare has remained at 30 cents since October 31, 1961. (Stip. 219) • • •

At a meeting on June 7, 1973, the New York and New Jersey Commissioners voted unanimously to increase the PATH fare from 30 cents to 50 cents because of increased operating costs, the 1972 deficit of $20,090,000 and the expectation that there would be no substantial increase in traffic. Neither of the Governors exercised his veto power over the proposed increase. During the following three months Governor Rockefeller of New York was enlisting support for the proposed $3.5 billion transportation bond issue in New York. A strong opponent of a prior New York proposed bond issue which failed, Mr. Theodore H. Kheel, publicly suggested that his prior strong support of the 1973 bond issue would be re-evaluated if Governor Rockefeller did not change his position regarding the proposed PATH increase. Governor Rockefeller sent Mr. Kheel a letter evidencing his support for only a 5 cents PATH fare increase and Mr. Kheel was quoted as saying that the New York Commissioners would "knuckle under to the Governor". *N.Y. Post,* September 26, 1973.

On September 21, 1973 Governor Rockefeller issued a statement to the effect that the PATH increase should be limited to 5 cents rather than the 20 cent increase approved by the PATH Commissioners and not vetoed by the Governors. At a meeting on September 26, 1973, all five New York Commissioners, contrary to their position four months earlier, voted to limit the proposed increase to 5 cents. The New Jersey Commissioners, however, voted in

the negative, and since a majority vote of the Commissioners of each state is necessary for Port Authority action, the proposed fare increase application remained at 20 cents. Mr. Kheel, however, continued his support of the 1973 New York Bond issue, and was quoted as stating that "I can't ask Governor Rockefeller to do more than deliver all the Commissioners of New York State, and that he did. . . ." *N.Y. Post,* September 27, 1973.

In February 1974, Commissioner Sagner appeared on behalf of Governor Byrne at the ICC Hearing on the PATH fare increase to state New Jersey's opposition to the PATH fare increase to 50¢. On February 14, 1974, following the stated opposition by Governor Byrne and Governor Wilson to the PATH fare increase, the Port Authority Commissioners voted unanimously to rescind their request to the ICC to approve the increase in the PATH fare. The PATH fare has remained at thirty cents. The present fare charged by the federally subsidized AMTRAK from Newark to Penn Station New York City is $1.00; the present Penn Central fare between those stations is $.75.

C. 1971 Bi-State Legislation

1. In April 1970, Governors Cahill and Rockefeller announced a joint program to increase the Port Authority's role in mass transportation by building a rail link to John F. Kennedy International Airport and extending PATH to Newark International Airport and other parts of New Jersey. According to the April 20, 1970 issue of *The (Newark) Evening News,* Governor Cahill said "one purpose of the legislation that will be introduced in both state bodies will be to erase the authority's impression that as long as the PATH system is operating at a loss the authority is absolved from any further responsibility for mass transit." Governor Cahill was also said to have noted that the Port Authority interprets the PATH legislation as absolving it from any further responsibility for mass transit and to have stated that the new bill will express "the intent of both legislatures that the PA do more in the area of mass transportation."

2. In March 1971, two days of joint hearings were held in New York and New Jersey by the New York State Assembly Committee on Corporations, Authorities and Commissions and the Autonomous Authorities Study Commission of the New Jersey State Legislature with respect to the relationship of the Port Authority to mass transportation. At the outset of the hearings, New York State Comptroller Levitt pointed out that the net revenues of the Port Authority increased from $68 million in 1961 to $115 million in 1970. During the ten-year period, the amount applied to interest on debt and scheduled long-term debt retirement ranged from $34 million to $54 million a year; over the ten-year period approximately $454 million in funds were available beyond interest and scheduled principal repayments and during the three prior years, approximately $55 million to $60 million a year was left. A large proportion of these moneys, almost $360 million, was applied by the Port Authority to capital construction through short-term borrowings.

Austin Tobin, then Executive Director of the Port Authority, testified at length concerning the history of the Port Authority and its credit requirements. Mr. Tobin noted that the Port Authority had been working on rail access to Kennedy Airport "for many years, and we have a concrete plan on that, that we are in the course of moving

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forward on it." With respect to a Newark Airport rail link, Mr. Tobin said, "there still might be some possibility in a PATH extension in some way, or in a Jersey Central extension. We are not optimistic on some of the PATH, we are not optimistic, and think that the other way would do a better job, but that is in the process." Mr. Tobin also stated that the PATH deficit "will go up to $30 million a year."

Mr. Tobin further stated that if the tolls on the Port Authority's bridges and tunnels were doubled, "I don't think we would lose many vehicles . . . my judgment is that you wouldn't, other than raising holy political hell, if we just looked at it from the traffic standpoint, it wouldn't affect much." Mr. Tobin said that if the tolls were doubled, the increased revenues to the Port Authority would be "between $50 million and $70 million." Mr. Tobin also stated that if the Legislatures "wish to change the nature" of the Port Authority and "give us the same type of State resources and back-up as the Metropolitan Transportation Authority has, and has to have, . . . we are ready to take on anything that you will give us the tools to work with, and be delighted. We will work within the public field, and it is just as much fun for us to run choo-choos as airports." Mr. Tobin further stated that various other authorities engaged in mass transportation such as the San Francisco Bay Authority, the Metropolitan Transportation Authority, the Chicago Authority, the Boston Area Authority and Authorities in Detroit and Montreal are all supported by the taxing power of the State. (Stip. 220-224) • • •

Assemblyman Koppell of New York referred to a report by the First National City Bank which suggested the appropriateness of imposing higher and economically more reasonable charges for the use of highways and river

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crossings in order to transfer badly needed added revenues to mass transit use. Mr. Tobin replied that "the penny surpluses from the tunnels and bridges are picking up the immense deficits from PATH." Mr. Koppell stated that the First National City Bank report specifically points out that tolls have been stable for 30 years and that the Hudson crossing tolls were fifty cents at a time when subway fares were a nickel; now subway fares cost six times as much*, while the tunnel and bridge tolls are the same. Mr. Tobin stated that an increase in bridge and tunnel tolls is opposed by every public official that is in any way concerned with traffic and that if the tolls were doubled, "it could not go under the law [to] mass transit anyway . . . we could use them for other facilities supported by the General Reserve Fund, but you could not, under the law and the constitution, use them for mass transit facilities." (Stip. 225-226) • • •

There was extensive discussion concerning the possible repeal of the 1962 Covenant. Assemblyman Koppell asked whether the Covenant could be repealed "not only for the future, but for the past" on the basis of the legislative finding "that in the exercise of our right to protect the people of the two states, we find that this covenant stands in the way of the proper development of mass transportation facilities, which is essential to the people's good and welfare." (Stip. 227-228) • • •

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* The subway fare as of December, 1974 is $.35 [footnote added by stipulation.]

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Charles Wodehouse, Chairman of the Railroad Committee and member of the Executive Committee of the New Jersey Citizens Transportation Council, stated:

> "It should go without saying that the continuing strangulation with which this area is faced due to clogged roads and lack of transit necessary to relieve that condition, absolutely must be met head on, and now, if the area is to survive as a job-producing, revenue-producing complex to support its population."

Mr. Wodehouse made "a special request that plans and action go forward without delay for high-speed transit for Newark and the New York Airports." (Stip. 229) • • •

3. The hearings included the following chart that had been submitted to the Farley Committee in 1961 with respect to the net revenues and investment of the Port Authority in each of its facilities as of December 31, 1960, together with the number of years that each facility operated at a loss.

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PORT OF NEW YORK AUTHORITY INVESTMENTS AND REVENUES

As Submitted to Senator Frank S. Farley, Chairman, New Jersey Senate Committee Created to Investigate the Port of New York Authority.
(000 Omitted)

	Total Investment		Net Revenues			
				Cumulative		
Facility	As of 12/31/60	After Completion of Constrn. Program Under Way	Year 1960	Amount	Yrs. in Svc.	Years in Deficit Oper.
N.Y. Intnl. Airport	$ 288,500	$425,000	$ 7,177	$ 16,966	14	7
LaGuardia Airport	27,205	90,000	(65)	1,123	14	7
Newark Airport	39,383	50,000	(527)	(9,296)	13	13
Teterboro Airport	10,540		(439)	(4,162)	12	12
Heliports	706		(103)	(288)	7	7
Grain Terminals, Grain Elevators, & Columbia St. Pier	3,734		(99)	1,040	15	3
Port Newark	62,249	125,000	498	4,908	13	3
Erie Basin Piers	8,930		266	405	3	—
Hoboken Piers	17,807		352	1,442	9	4
Brooklyn Piers	60,971	90,000	(197)	(431)	5	4
Elizabeth	9,452	150,000	(Not yet in operation)			
PA Building	22,457		636	(3,040)	28	21
N.Y.Truck Terminal	9,923		(284)	(5,459)	11	11
Newark Truck Term.	8,120		(391)	(2,065)	11	10
N.Y. Bus Terminal	26,272	45,000	(4)	(5,476)	11	11
Holland Tunnel	57,950		3,049	82,871	30	—
Lincoln Tunnel	184,062		(83)	16,357	24	10
Geo. Washington Br.	143,680	260,000	9,207	99,424	30	8
Staten Isl. Bridges	30,590	45,000	209	(14,724)	33	22
Total	$1,012,500		$19,202	$179,592		

Note: Parentheses denote deficits.

(Stip. 231-232) * * *

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5. In June 1971, the Legislatures of New York and New Jersey enacted legislation authorizing the Port Authority to extend passenger rail transportation to Kennedy International Airport and to Newark International Airport and Cranford (Chapter 245, Laws of New Jersey of 1971). While this legislation was pending, the Port Authority obtained opinion letters from the New York firms of Hawkins, Delafield & Wood (May 3, 1971) and Davis Polk & Wardwell (June 3, 1971), which concluded that the proposed rail extensions were subject to the provisions of the 1962 Covenant (and could not be financed out of Port Authority revenues or reserves unless "self-supporting"—PATH alone having used up all of the "permitted deficits") even if the Legislatures were to amend the statutory definitions of "air terminals" (1947 Laws of New York, Ch. 802, §3; N.J.S.A. 32:135.3) so as to bring the proposed rail extensions within those definitions. (Stip. 233) • • •

7. On December 8, 1971, the First Boston Corporation, having been commissioned to do so earlier in 1971 by the Port Authority, issued a Passenger Rail Transportation Study. In analyzing the proposed airport rail links, First Boston noted "The essential problem which is posed by these undertakings is created in the statutes and resolutions by which the Port Authority is bound; and particularly the joint State covenants of 1962, which in effect prohibit the Port Authority's involvement in additional passenger transportation projects unless they are self-supporting." According to the First Boston Study the 1962 Covenant "precludes general credit financing of any passenger transportation project, no matter how desirable, for which projects show an operating profit below debt service requirements." Since federal funds could be provided only

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for construction of new facilities on a matching basis and not for operating expenses, "any project would have to cover its operating and maintenance costs and a large portion of debt service from the fare box." The study stated that the project could be financed by the Port Authority under existing statutes and resolutions if:

> "(1) it were self supporting, or
>
> "(2) if a legal opinion is obtained (which may require litigation) supporting either theory under (A) and (B) above [the "airport adjunct" theory or a theory that financing of passenger rail mass transit could be considered "to or for the benefit" of Consolidated Bondholders], or
>
> "(3) the project does not incur (along with present PATH deficits) an aggregate annual deficit in excess of 10% of the General Reserve Fund.
>
> "This third approach opens three possibilities:
>
> "(A) Application of federal urban passenger rail transportation projects. The Urban Mass Transportation Act of 1970 provides for sizeable grants for acquisition or construction of new facilities on a matching basis; grants, however, are not to be applied to operating expenses. Therefore, any project would have to cover its operating and maintenance costs and a large portion of debt service from the fare box. Depending, however, on the particular project's projected revenues and the grants obtained, the Port Authority might be able to effectuate pas-

senger rail transportation projects with such assistance. In particular, airport rail links could probably benefit from these grants, but, once again, their costs would have to be detailed to determine if, with these grants, they would be self-supporting or within the 10% aggregate deficit limitation.

"(B) An increase of PATH fares to a level sufficient to cover the present and projected PATH deficits, thus permitting an amount equal to 10% of the General Reserve Fund moneys to be applied to other passenger rail transportation projects. The PATH per-passenger loss for 1970 was approximately 35¢. If the PATH fare were increased by this much, assuming that future traffic patterns and operating expenses were to remain the same, there would be no deficit at all resulting from PATH operation, and the Port Authority might incur up to an annual deficit of about $12.7 million on other passenger rail transportation projects. Although a 35¢ increase is impractical, any increase up to that amount would free a proportional amount of the 1962 mass transit limitation as measured by 10% of the General Reserve Fund for use in other passenger rail transportation projects. Because annual deficits of PATH have been increasing over the years since its acquisition (e.g., an increase from $10.9 million to $12.3 million for 1968 to 1969 and from $12.2 million to $13.2 million for 1969 to 1970), fare increases would probably need to be escalating, depending on the rate of PATH expense increases. The importance of the ability of the Port Authority to raise fares on PATH to reduce the deficits below the statutory maximum can only be determined after the cost and engineering figures on the proposed rail links are completed and any resulting deficits are known.

"(C) Use of additional financing capacity engendered by growth of the General Reserve Fund. At the rate of future financing contemplated by the Port Authority, the General Reserve Fund will grow at about $10 million per year—this means that about $1 million per year would be added to the allowable annual deficit to be incurred in passenger rail transportation projects. Even if deficits of PATH were not to increase over the next few years, this contribution alone is really too small to enable significant participation by the Port Authority in deficit passenger rail transportation projects."

"We do not have enough information on the Airport rail link project to quantify whether the dollars which might be released for deficit passenger rail transportation under (A), (B), (C) or a combination thereof would represent a sum of money sufficient for successful completion of the project."

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The study also discussed two ways of financing beyond the provisions of current resolutions and statutes. One involves the imposition of what might be called a mass transportation "surcharge" and the other involves use of funds already being generated by the Port Authority. Each, however, would require 60% approval of the aggregate of outstanding Consolidated Bond holders. The study discussed three programs, one of which falls in the first category, and the other two in the second, as follows:

"(1) Increase the tolls on all Port Authority bridges and tunnels by some percentage, say 50%, and deposit the revenues into a 'transportation fund', this fund to meet debt service on a series of bonds financing passenger rail mass transportation. (A portion could be retained to cover expenses of the program.) This diversion of funds would require approval of 60% of the Consolidated Bond holders, in that the use of these funds for passenger rail transportation purposes is prohibited by the 1962 Covenant and is limited by the Series Resolution of each issue of Consolidated Bonds.

"The States of New York and New Jersey would then guarantee to the Port Authority *any difference between gross revenues collected after toll increases and higher gross revenues collected before toll increases.* This would bring into being a State financial contingent liability and would require legislative authorization; a *direct* guarantee of revenues creates a debt on the part of the state and would require a voter referendum and legislative

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action in New Jersey and a constitutional amendment (which itself requires approval of two successive legislatures before submission to a voter referendum) in New York; a moral obligation similar to that of the New York State Urban Development Corporation or New York Housing Finance Agency to make up the difference in revenues would not require such extensive legislative action and voter approval but would only require approval by both legislatures. Therefore, a law providing for a direct guarantee by the States would probably take 18 months or more to enact, whereas moral obligation could be obtained much faster. There is not much of a possibility that such an obligation would have to be honored unless traffic patterns were temporarily altered because of the fare increase, or unless automobile traffic patterns generally in and out of New York City were to change radically, perhaps not immediately but conceivably in the next 10 or 20 years. In this regard, the New York State Comptroller has asked assurances before lending his support in the cases of moral obligation created heretofore that these obligations have only the remotest possibility of being honored. It should be noted that a 50% increase in tolls would produce approximately $40,000,000 of additional revenues and, thereby, $430,000,000 in debt issuing capability. These figures are based on 1970 traffic and, while an increase in the fare might temporarily level off

or reduce traffic, use of these facilities should increase in the years ahead.

"The $40,000,000 of additional revenue projected to permit about $430,000,000 of debt capital is based on a 6% interest cost, the debt to mature in approximately 40 years, and the approximate $40,000,000 annual transportation surcharge to cover annual debt service 1.4 times. The facts that the Port of New York Authority will continue to retain its current income ($1.00 round trip) on the bridges and tunnels, that there would be a two-State moral guarantee these revenues will not decrease from their recent highest levels, and there is the probability of increase in these revenues through additional traffic, should enable the Port of New York Authority Consolidated Bonds to remain a highly rated investment security. Since the Consolidated Bond Reserve Fund and the General Reserve Fund have been left intact for building the equity for future Port projects, this plan might be more palatable to the present holders of the Port Authority Consolidated Bonds than would the next plan discussed.

"The major advantage of this plan is that the bonds secured by these toll increases would sell readily; their security, of course, would depend on tunnel and bridge traffic, but the new bonds would have a first lien on any increased amount of fares of these facilities.

"There are several drawbacks to this approach, however: (a) a monetary inducement (similar to that required in Triborough Bridge experience) would be necessary simply to make bond holders 'go to the trouble' of consenting to the amendment by sending in their proxy statement. This consideration would be affected by the distribution of the issue. (b) The difference made up by the States might dwindle since gross revenue guarantees do not provide for the increases in operating expenses incurred in operation of the bridges and tunnels. An additional fare increase might therefore be required to provide sufficient coverage to permit issuance of any additional Consolidated Bonds. (c) The Port Authority would give up some of its financial independence from the States and could be placed in competition with other State agencies for legislative appropriations. (d) The proceeds of the fare increase would have to be used for limited and specific interstate transporation [sic] purposes to avoid 'head tax' problems.

"(2) An alternative plan, which would not involve state action, involves restructuring the present Consolidated Bond Reserve Fund into a limited size fund (similar to the General Reserve Fund) with excess revenues to flow to a new 'Transportation Fund' to be pledged to debt service on a 'Transportation Bond' series. The level chosen for the Consolidated Bond Reserve Fund may be a fixed one, or on some

sliding scale, as is the General Reserve Fund. The size of the Transporation [sic] Fund created would be fixed also as determined by projects to be undertaken. The flow-through of funds would require approval of 60% of aggregate bond holders, because the use of these funds for passenger rail transportation purposes is prohibited by the 1962 Covenant and is limited by the Series Resolution of each issue of Consolidated Bonds. As in the previous case, some monetary inducement would have to be offered to present bond holders to obtain their consent; once again, the percentage increment in coupon rate would be determined by the distribution of the issues and by the coupon of each Series. It is important to note that all Port facilities would be contributing to the excess revenue flow. (In 1970 excess available revenues of the Port Authority were $30 million.) However, it should be noted that some of this excess is already pledged to bank loans. This would permit, upon termination of the bank loan agreements, flexibility on the part of the Port Authority Commissioners and the Governors of the two States; if a greater involvement in mass transportation were deemed necessary, tolls, fees, or other charges might be increased (subject in some cases to approval by the U. S. Secretary of Transportation) without recourse to the State legislatures. A careful analysis of projected revenues is, of course, necessary to

ensure that debt service on Consolidated Bonds would be covered, and that there would still be a sufficient flow into the Transportation Fund to permit coverage of debt service on passenger rail transportation bonds. This alternative will stand up only if there is sufficient flow of revenues to provide a sizable Transporation [sic] Fund from year to year. Potential bond holders must be assured from projections that the Port Authority can flow through revenues as necessary to meet debt service. Because of the second lien aspect these bonds might be more difficult to sell than those of the first alternative. In addition, assurance must be provided to present bond holders that their security will not be diluted by too many unprofitable projects. Historical revenues (see Exhibit 1), furthermore, show that the Port Authority would be able to support approximately the same amount of passenger rail transprotation [sic] debt (without any toll increase) under this plan as it would with a bridge and tunnel toll increase under the previously described plan. While the fare and toll increases of 50% might bring in approximately $40 million annually (not allowing for increase in operating expense, consequent further toll increase, and possible traffic dropoff), Exhibit 1 shows the excess revenues from all facilities to be about $30 million in 1970.

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"If an annual amount of $30 million continued to be available for debt service on transportation bonds, then, at a rate of 6%, about $325,000,000 in debt could be supported at a coverage of 1.4 times debt service. This figure does not give consideration to the possible growth in Port Authority normal operating revenues, and the potential savings in current debt charges which might be saved by extending the maturities in refunding part of the bank debt.

"(3) A third solution would involve a bi-State guarantee of the level of the General Reserve Fund, such that all Consolidated Bond holders would benefit thereby. This would be a moral obligation of the New York State Urban Development Corporation type, and would allow use of funds by the Port Authority at its discretion. This course of action would essentially be a guarantee of the payment of the Port Authority's debt service, since the General Reserve Fund is maintained from net revenues after debt service. It is felt that bond holder approval of expenditure for rail purposes would *still* be required in the selection of this alternative. The States' contingent liability would be significantly greater with this approach, and therefore this alternative is the least attractive of the three as to Port Authority autonomy, although perhaps the most appealing to present bond holders." (Stip 242-251) * * *

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9. In June 1972 it was reported that on the basis of an engineering cost study by Louis T. Klauder & Associates, the Port Authority and New Jersey Department of Transportation concluded that the proposed extension of PATH via Newark Airport to Cranford was not economically feasible under the terms of subparagraph (b) of the 1962 Covenant. Under the Cranford Plan, the Central Railroad of New Jersey would have continued its commuter operations into Newark from points west of Cranford and would have competed with the Cranford service proposed for PATH.

10. In June 1972, the State of New York passed a bill repealing the 1962 Covenant. Ch. 1003, Laws of N.Y. 1972. Governor Rockefeller's message on the signing of that legislation stated:

"I am approving this bill in order to give incentive to the Port of New York Authority to proceed with urgently needed mass transportation facilities in the metropolitan region.

"Passed with overwhelming bipartisan support in both houses of the Legislature, the bill removes the absolute statutory prohibition against the use of the revenues of the Port of New York Authority for railroad purposes. That statutory covenant, together with the provision of the bi-state compact creating the Authority that neither State will construct competing facilities within the Port District, could forever preclude the two states from undertaking vitally needed mass transportation projects. In removing the present restriction, the bill would

not jeopardize the security of Port Authority bondholders or their rights to maintain that security.

"My signature on this bill does not make it law unless the same measure is adopted by the Legislature and approved by the Governor of New Jersey. In the period immediately ahead, I shall be working with New Jersey on this question and will be prepared to suggest and approve amendments to the bill which would preserve the traditional high reputation of the Port Authority's obligations within the investment community. I would be prepared to submit such amendments either in the next regular session of the Legislature or, if the need arises, at a special session. In the interim, the Commissioners of the Port Authority can proceed with urgently needed mass transportation projects and the construction of the other vital construction activities in which the agency is engaged.

"New York, by the enactment of this measure, is taking an essential step in its long-range effort to realize the full potential of the Port Authority in meeting the total transportation needs of the New York-New Jersey port district. The Port Authority's active participation in helping to solve the problems of mass transportation in the New York City metropolitan area will inure to the benefit not only of millions of area residents generally, but also to the port facilities operated by the Authority and the workers and businesses that rely on them. This bill is consistent with the original purpose of the Port Authority—to ensure the coordinated development

of terminal, transportation and other facilities of commerce in and about the port district for the greater benefit of the people of New York and New Jersey.

"The bill is approved.

Nelson A. Rockefeller"

McKinney's Session Laws of N.Y., 1972 at 3411-12. The State of New Jersey failed to approve the necessary concurrent legislation.

D. The November 1972 Governors' Agreement

1. On November 15, 1972, following a series of meetings among Governors Cahill and Rockefeller and the Commissioners of the Port Authority, the Governors announced agreement on a bi-State plan of major rail mass transportation development by the Port Authority. The Plan provided for the extension of PATH via Newark Airport to Plainfield, direct rail service from Kennedy Airport to New York City and direct rail service to Penn Station, New York for riders of the Erie Lackawanna Railroad in 6 northern New Jersey counties and 2 counties in New York. The estimated total cost of the plan was $650,000,000 and it was estimated that the Port Authority would invest between $250,000,000 and $300,000,000. The Governors also proposed to eliminate subparagraph (b) of the 1962 Covenant with respect to bonds issued subsequent to the enactment of the legislation proposed by the Governors. (Stip. 251-253a) • • •

2. On December 11, 1972 the New Jersey Senate held an information session to consider the Port Authority mass

transit bills. • • • Representatives of the Port Authority and of Governor Cahill's office stated that the State of New Jersey would have to commit substantially all of the funds then available to the State of New Jersey from the federal Urban Mass Transportation Administration and, in addition, advance $40,000,000 of its own funds to be repaid over the 30-35 year life of the Plainfield project. (Stip. 253a) • • •

3. The legislation embodying the 1962 Covenant was amended effective May 10, 1973 by the States of New Jersey and New York (Chs. 207 and 208, Laws of New Jersey of 1972, Ch. 1003, Laws of New York of 1972, Chs. 317 and 318, Laws of New York of 1973), to repeal subparagraph (b) of the 1962 Covenant with respect to bonds issued after the date of the legislation. Section 3 of the New Jersey statute provided:

> "The amendment made by section 2 of this act [the repealer] shall not take effect with respect to the covenant and agreement made by the States of New York and New Jersey in clause (b) of the first paragraph of section 6 of both chapter 8 of the laws of New Jersey of 1962 and chapter 209 of the laws of New York of 1962 with the holders of 'affected bonds' (as defined in said section 6) issued and outstanding and unpaid on the effective date of this act." § 3, Ch. 208, Laws of N.J., 1972; N.J.S.A. 32:1-35.55(a).

The introductory statement appended to the New Jersey bill provided:

> "This bill provides that an extension of rail transit lines between the city of Newark and the city of

Plainfield shall be part of the Hudson tubes extensions.

"In addition, the bill authorizes improvements to railroad lines connecting with PATH to provide for connections between passenger lines and branches of the Erie-Lackawanna Railroad and the Penn Central Railroad. This will result in improved rail transit service and direct access to and from midtown Manhattan for commuters and residents of Bergen, Essex, Passaic, Morris, Somerset and Union counties in New Jersey and Rockland and Orange counties in New York State.

"The bill is also designed to preclude the application of the 1962 covenant to holders of bonds newly issued after the effective date of this act, while maintaining in status quo the rights of the holders of the bonds issued after March 27, 1962 (the effective date of the 1962 covenant legislation) but prior to the effective date of this act."

4. Port Authority Consolidated Bonds issued prior to May 10, 1973 have varying maturity dates from 1993 to 2007 (unless earlier redeemed).

5. The Erie Lackawanna Direct Access Plan referred to [above] involves the construction by the Port Authority of connecting tracks to Penn Central in Kearny for the Erie Lackawanna Morris & Essex line and in Secaucus for the Bergen County, Pascack Valley and Main lines of the Erie Lackawanna, the construction of a new bridge over the Hackensack River and the construction of a new railroad yard as well as major improvements to Penn Station,

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New York. Under this proposed service, Erie Lackawanna riders could either go directly to Penn Station in mid-Manhattan or continue to transfer at Hoboken to PATH for lower Manhattan. At present, there is no direct ride into Manhattan for any Erie Lackawanna rider. (Stip. 256-257) • • •

8. During the December 1972 information session conducted by the New Jersey Senate the Port Authority proposed to finance the $150,000,000 estimated costs of the Lackawanna program by means of a $100,000,000 federal grant charged to the State of New Jersey and the issuance of $50,000,000 of Port Authority bonds. The debt service on the Port Authority bonds would be financed by making available to the Port Authority a through charge approximately equal to the existing PATH fare at the time of implementation of the direct service plan. The Erie Lackawanna would be responsible for collecting the through charge either from its passengers or from the operating subsidy paid to the Erie Lackawanna by the State of New Jersey. On this basis its was stated that this proposed plan could be effected within the terms of the 1962 Covenant.

9. The PATH extension to Plainfield via Newark Airport was projected during the December 1972 information session to involve capital costs of $240,000,000, of which $150,000,000 would be in the form of a federal grant charged to the State of New Jersey, the Port Authority would invest $50,000,000 and the State of New Jersey would advance $40,000,000. Louis Gambaccini, Director of the Department of Rail Transportation of the Port

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Authority, stated that the Port Authority expected this project to be "barely doable on a self-supporting basis" assuming that these capital funds were available only because the Plainfield project would take over the major portion of the service provided by the Central Railroad of New Jersey and because additional passengers could be served through the construction of a park-ride facility near the Garden State Parkway and by routing the Plainfield extension to a point from which it could serve Newark Airport. Debt service and operating expenses incurred in connection with the Plainfield project would be obtained by PATH directly from passengers on the assumption that the user of the proposed rapid transit service would pay approximately the same fare as was charged by the Central Railroad of New Jersey.

The State of New Jersey's commitment to advance up to $40 million of the necessary financing is evidenced by the following letter, dated August 10, 1973, from the Governor of New Jersey to the Chairman of the Port Authority:

"Dear Mr. Chairman:

"As you know, New York has now enacted legislation identical with our Chapters 207 and 208, P.L. 1972. The Port Authority is thus authorized, inter alia, to:

"(1) Construct improvements providing for direct rail service to Pennsylvania Station, New York, and

"(2) Provide as a Port Authority Trans-Hudson System (PATH) extension rail link between Newark International Airport and Penn Station, Newark, between Newark International Airport and Plainfield, New Jersey, which will also provide service between Plainfield and Newark.

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"The projects are more precisely defined in the laws cited above.

"When I joined with Governor Rockefeller in announcing these plans in November, we stated that these plans anticipated that federal mass transit and airport aid funds would be available to cover a substantial portion of the capital improvement costs with the remainder to be covered by Port Authority funds, revenues from the projects and state capital contributions.

"As to the direct rail links of the Erie Lackawanna to Penn Station, New York, you will recall that we contemplate no state contributions and rather envision the amortization of your capital cost (net of Federal Aid) through operating revenues. The PATH extension does, however, involve capital contributions by the State of New Jersey. In this connection it is important to note that this project will obviate significant programmed capital expenditures by the State in connection with Central Railroad of New Jersey main line improvements and that increasing operating subsidies being paid by the State to that railroad will be substantially reduced when the new program has been completed.

"Although the necessary agreements to effectuate all the matters referred to in this letter will be prepared over some period of time, I know that it is essential to your planning that the State of New Jersey confirm its intention to assume a portion of the costs as outlined below. For example, I understand that the Port Authority is presently preparing

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preliminary applications to the U.S. Department of Transportation for urban mass transportation funds. It is for that reason that I am sending this letter to you today.

"We have agreed that the State of New Jersey will advance up to $40 million for its share of the capital cost of the PATH extension project. I understand that you have included in the capital cost of this project the cost of all labor protective agreements which may be required under the Urban Mass Transportation Act such as for Central Railroad of New Jersey employees. The capital contribution of New Jersey would be paid over to the Port Authority at the time the project is certified. I understand that the agreement with respect to this advance will provide for repayment to the State of New Jersey from net project revenues after the operation and maintenance and debt service charges have been satisfied.

"While I look to the Port Authority to negotiate for all necessary operating rights, particularly those over the Central Railroad of New Jersey property, I recognize that the successful implementation of the project requires that the C & J operating rights be acquired at minimal cost. I have pledged the State's complete cooperation in achieving this end.

"As was always contemplated, the State of New Jersey will cooperate fully in securing the necessary Federal aid. To this end the State will act as Federal aid sponsor for the project designed to improve direct access to Pennsylvania Station, New York.

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"The State will also cooperate with respect to securing Federal aid for the PATH extension project, subject only to our approving the preliminary and final Federal aid application prior to submission. Obviously we must reserve this right of approval since the exact amount of our contribution could be less than $40 million if a substantial portion of this project could be finally qualified or characterized as an adjunct to the Newark International Airport.

"I trust the Port Authority will continue to progress the planning and design of these projects so that they may be implemented as quickly as possible to the benefit of the people of New Jersey.

Sincerely,

/s/ William T. Cahill
GOVERNOR"

(Stip. 258-262) • • •

10. The 1973 [New Jersey Department of Transportation Transit Development] Program stated:

> "The key to the long-range development of the public transportation plan in the [Hunterdon-Somerset-Middlesex-Union Counties] corridor is the extension of the Port Authority Trans-Hudson (PATH) rapid transit system. It is anticipated that PATH will be extended from its present terminus at Penn Station, Newark to Newark Airport and a proposed transportation center terminal in Plainfield, Union County. The commuter rail operations of the Central Railroad of New Jersey and the Reading will be restricted to points west and south of Plainfield. Commuter bus operations will be realigned to provide feeder service from communities in the PATH service area and various points to the west of Plainfield.
>
> "The institution of PATH service will revitalize the public transportation in the corridor and provide an attractive alternative to the private auto for journey-to-work trips. It is anticipated that PATH will reverse the downward ridership trend in both rail and bus modes. The complementary connecting service will be provided west of Plainfield along the CNJ Mainline and the Reading Company trackage. . . . (Stip. 266-267) • • •

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11. A booklet concerning the PATH-Plainfield project, issued by PATH in January 1974, contained the following information "underlin[ing] the importance of the proposed PATH extension":

> "The growth and development of communities along the CNJ Mainline have been spurred directly by the presence of the railroad. They are primarily residential in nature, with a large number of journey to work commuters. The 7,800 passengers who commute each day to Newark and New York City on the CNJ Mainline represent a key economic asset to their communities, earning an estimated $100 million annually.
>
> "Highway access to this Corridor is extremely inadequate and the area traditionally has needed high capacity transit services. The area continues to be strongly dependent on the CNJ service, supplemented by several commuter bus lines.

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"Further, the communities in the Corridor, particularly Plainfield, are counting heavily on continued rail service to spur redevelopment programs in the older sections and support the economic health of the entire area.

"The plight of the CNJ, highway congestion, the energy crisis, and the need for continued economic development underline the importance of the proposed PATH extension.

"Substantial benefits will accrue to Newark and Elizabeth as a result of the PATH project. Most important for Newark is direct rail access to Newark International Airport. Although economically unfeasible in the past as a separate service, the changed economics of the Plainfield Service Corridor Project now make airport access possible.

"This rail access will provide increased accessibility to job opportunities for Newark's large work force and will enhance Newark's function as the regional center of commerce and industry. Further, the area adjacent to PATH's Newark International Airport/McClellan Street station will offer Newark opportunities for airport-related development in conjunction with its planned redevelopment programs.

"Elizabeth's Central Business District also will benefit from direct rail access to the airport, which will be only four minutes away on the PATH extension. Elizabeth's business community and residents further will benefit from the inauguration of direct rail rapid transit service into Lower Manhattan. . . .

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"This project will provide significant economic benefits to the entire area from Newark to Plainfield and beyond. The communities along the right-of-way will benefit from improved transit service and the new advantage of direct airport access. This will enhance property values in suburban communities which have developed along the rail right-of-way and stimulate the economic growth of the urban centers. Job opportunities will be created on the transit system and its related facilities and within the off-airport satellite development which is expected to develop. In addition, during the development period, construction will be a significant source of employment for skilled and semi-skilled labor. . . .

"The project is complementary to the anticipated land development in the Plainfield Corridor and consistent with actual or planned land use. This is primarily because communities along the right-of way have developed adjacent land uses in harmony with existing railroad passenger and freight operations. The primary impact will be one of environmental conservation by maintaining and upgrading rail service in the Corridor.

"Based on 1985 traffic estimates, the PATH extension to Plainfield will generate about 9 million automobile and bus miles in travel to and from Corridor stations. By contrast, if rail service is abandoned in the Corridor, an estimated 46.5 million auto and bus miles would be required yearly on the roads leading to Newark and New York City. The saving of 37.5 million vehicle miles per year will result in less highway congestion and less air pollution. In

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addition, it will be far more efficient in terms of the utilization of scarce energy resources. . . .

"The estimated gross project cost of the Plainfield Corridor Service Project is $221,510,000, which will be financed in part by an 80 per cent capital grant under the Federal Urban Mass Transportation Program. The 20 per cent local contribution will be provided by the Port Authority Trans-Hudson (PATH) Corporation, through funds of The Port Authority of New York and New Jersey and, if necessary, by a financial advance from the state of New Jersey to be repaid by The Port Authority.

"The PATH extension to Plainfield is planned to be achieved on a financially break-even basis, thus permitting the taxpayers of the State of New Jersey to be relieved of all subsidy obligations for CNJ service in this area. Further, the State will not have to bear the responsibility for capital improvement programs which had been identified for the CNJ in the Corridor.

"Due to the inherent deficit nature of the existing PATH system and legal constraints on the Port Authority, the project cannot be accomplished without the assistance of the Federal grant."

On April 1, 1974 PATH submitted an application to the federal Urban Mass Transit Administration for a capital grant in the amount of $201,527,000 to cover 80 per cent of the capital costs of the Plainfield project. That application has been deferred. (Stip. 267-270) • • •

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12. • • • On October 24, 1974, Frank C. Herringer, the Administrator of UMTA, stated that his agency had deferred action on the application for approximately $200 million in UMTA funds for the PATH-Plainfield project because the application submitted by the Port Authority in April 1974 failed to include a certification of how the local financial share of approximately $50 million would be obtained. According to Administrator Herringer, the Port Authority had been advised of this deficiency in June 1974, but had not responded to this advice.

IV. Federal Mass Transportation Policy

• • •

3. In July 1964, Congress enacted the Urban Mass Transportation Act of 1964 (49 U.S.C. §§1601 et seq.), expressing for the first time a federal legislative interest in the support of urban mass transportation systems. In enacting the 1964 act, Congress found (49 U.S.C. §1601 (a)):

"(1) that the predominant part of the Nation's population is located in its rapidly expanding metropolitan and other urban areas, which generally cross the boundary lines of local jurisdictions and often extend into two or more States;

"(2) that the welfare and vitality of urban areas, the satisfactory movement of people and goods within such areas, and the effectiveness of housing, urban renewal, highway and other federally aided programs are being jeopardized by the deterioration or inadequate provision of urban transportation facilities and services, the intensification of traffic

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congestion, and the lack of coordinated transportation and other development planning on a comprehensive and continuing basis; and

"(3) the Federal financial assistance for the development of efficient and coordinated mass transportation systems is essential to the solution of these urban problems."

The purposes of the 1964 act were declared to be (49 U.S.C. § 1601(b)):

"(1) to assist in the development of improved mass transportation facilities, equipment, techniques, and methods, with the cooperation of mass transportation companies both public and private;

"(2) to encourage the planning and establishment of areawide urban mass transportation systems needed for economic and desirable urban development, with the cooperation of mass transportation companies both public and private; and

"(3) to provide assistance to State and local governments and their instrumentalities in financing such systems, to be operated by public or private mass transportation companies as determined by local needs."

4. The scope of the 1964 Act was expanded by the Urban Mass Transportation Assistance Act of 1970 on the basis of a finding by Congress (49 U.S.C. § 1601a) "that the rapid urbanization and the continued dispersal of population and activities within urban areas has made the ability of all citizens to move quickly and at reasonable cost an urgent national problem."

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5. In November 1974, Congress enacted the National Mass Transportation Assistance Act of 1974, which provides $11.8 billion over the next 6 years for mass transit capital expenditures and, for the first time, operating subsidies. Of the $3.975 billion in federal funds for operating subsidies provided by the Act, New Jersey would receive approximately $177 million, New York City would receive $563 million and the rest of New York State would receive $101 million. The federal operating subsidies are required to be matched by an equal amount of State or local tax revenues used for mass transit operations or the undistributed cash surplus, replacement or depreciation funds, cash reserves or new capital provided by a public or private transit system.

The Act contained the following findings by Congress:

"(1) over 70 per centum of the Nation's population lives in urban areas;

(2) transportation is the lifeblood of an urbanized society and the health and welfare of that society depends upon the provision of efficient, economical and convenient transportation within and between its urban area;

(3) for many years the mass transportation industry satisfied the transportation needs of the urban areas of the country capably and profitably;

(4) in recent years the maintenance of even minimal mass transportation service in urban areas has become so financially burdensome as to threaten the continuation of this essential public service;

(5) the termination of such service or the continued increase in its cost to the user is undesirable,

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and may have a particularly serious adverse effect upon the welfare of a substantial number of lower income persons;

(6) some urban areas are now engaged in developing preliminary plans for, or are actually carrying out, comprehensive projects to revitalize their mass transportation operations; and

(7) immediate substantial Federal assistance is needed to enable many mass transportation systems to continue to provide vital service."

On November 19, 1974, during the Senate debate with respect to the Act, Senator Williams, one of the principal sponsors of the Act, stated:

"As we all know, last winter's shortage of petroleum products created a crisis situation in the United States. We have seen gas station closings, long waits to obtain fuel, complex allocation formulas and the possibility of eventual rationing. And this winter we may once again be confronted with a similar situation.

"One of the ways in which we can combat the energy shortage is by improving urban mass transportation. . . .

"If we are to alleviate the energy crisis, remove traffic congestion and the environmental pollution which results, existing transit systems must be kept in operation, their services expanded and new ones must be built. . . .

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"Now there is a great national stake in maintaining and improving our Nation's mass transit programs.

"The issue of mobility and the quality of life afforded thousands upon thousands of our citizens who must depend upon urban mass transportation is at stake.

"To take no action in response to the combined transit and energy crisis would be to condone further deterioration."

Congressman Minish, another of the principal sponsors of the Act, stated:

"[W]ith our present energy situation and the threat of a renewed crisis in this area, the need for mass transit aid has become ever more critical. Buses and rail cars consume only a fraction of the energy that a private automobile does, yet we cannot expect the commuting public to reduce significantly its use of private cars if we do not provide suitable alternative sources of transportation.

"In conclusion, let me say there is a great national stake in maintaining and improving our mass transit systems. The issue here is the quality of life afforded to millions of our citizens. To take no action at this point, or to defer action, would be, in effect, to condone further deterioration of our environment, our energy status, and our quality of life. This must not be permitted to happen."

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Other Senators and Representatives expressed their support for the position of Senator Williams and Representative Minish.

Representative Abzug, speaking in support of the Act, stated:

> "This [Federal] commitment to aid and expand existing mass transit systems and develop new ones is an essential ingredient of a rational Federal policy on energy use, economic development in the large urban areas as well as rural areas, and protection of the environment. . . .
>
> "This bill represents a commitment toward the principle of operating subsidies and recognition of the fact that highway spending is the most expensive way to move the least number of people, at a terrible price to masses of our citizens, the viability of our cities, and the quality of our environment.
>
> "Increased mass transit assistance is needed not just as a political response, but as an urgent initiative. It is needed not just to prevent long lines at the gas stations but for the positive good that it can create.
>
> "Transportation affects every segment of our economy and our lives. It affects where people work and what kind of jobs they can get. For the carless poor, it means very basically the right to work because without public transit they cannot get to their jobs. In rural areas, the complete absence of transit services means that the poor cannot have access to health clinics, educational opportunities and jobs.

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> In the cities, it means that low-income groups, the handicapped, the elderly, and the young, all those who are transit dependent, cannot enjoy the quality of life shared by those who drive. In the cities, too, the existence of highways alone, without comparable mass transit facilities, serves as a dividing line dictating housing patterns, creating ethnic concentrations and preventing social mobility. . . .
>
> "This bill is expected to provide $170 million of the $200 million in operating subsidies sought by New York City for this fiscal year to maintain the fare at its present level. It would also provide the city with $125 million for capital expenditures in the same period.
>
> "It will now be up to the new Carey administration of New York State and the Beame administration in New York City to provide the additional funds to hold the fare at 35 cents, and I am certain that they will make every effort to do so. If it is necessary to place tolls on bridges within New York City to raise the additional funds, then this should be done, but under no circumstances can the people of New York City afford to pay any more money for the basic necessity of transportation. I also support the proposal by Governor Byrne of New Jersey for an independent investigation into the finances and operations of the New York Port Authority, which should be using its huge reserves to subsidize and develop mass transit lines within the metropolitan New York area."

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6. Tolls charged on the Port Authority's vehicular tunnels are not regulated by the Federal Government. The tolls charged on the interstate bridges of the Port Authority are subject to the terms of the Bridge Act of 1906 (34 Stat. 84, 33 U.S.C. §491 et seq.), which provides that the tolls charged "shall be reasonable and just" and that the Secretary of War [later the Secretary of the Army and still later the Secretary of Transportation] shall have the power at any time and from time to time to prescribe such rates. This power is presently delegated by the Secretary of Transportation to the Federal Highway Administrator (32 F.R. 5607, 49 C.F.R. §1.48(i) (1)).

The Secretary of War in 1937 and the Secretary of the Army in 1947, 1948, 1949 and 1950 have rejected complaints asking for a reduction of the basic $.50 toll charged for the use of Port Authority bridges. (Stip. 274-280) • • •

7. • • • On October 16 , 1974, an Administrative Law Judge issued a decision (*Matter of the Walt Whitman and Benjamin Franklin Bridge Tolls*) recommending that the Federal Highway Administrator find that the tolls presently being charged on the Delaware River Port Authority crossings are not "just and reasonable" under the General Bridge Act of 1946 and should be reduced.

The controversy over DRPA's tolls began in April of 1972 when the Authority increased the one-way automobile toll from 50 cents to 60, the commuter toll from 25 cents to 35, and the rate for buses and trucks from 50 to 75 cents per axle on its Benjamin Franklin and Walt Whitman Bridges linking New Jersey with Philadelphia.

Exercising his authority under Federal Laws to ensure reasonable tolls, the Highway Administrator ordered a public hearing held on the DRPA toll increases. Thereafter, in December, 1972, the then presiding Law Judge decided that the new tolls on the Delaware River Port Authority crossings were not just and reasonable and recommended that they be rolled back to the pre-April 1972 levels. (Stip. 281-281a) • • •

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DRPA appealed to the Federal Highway Administrator who on November 5, 1973 issued an opinion and order sustaining the toll increases for commuters and trucks, but ordering the rollback to their pre-April 1972 levels of the one-way automobile toll and bus tolls.

The opinion of the Federal Highway Administrator stated:

> "It is not necessary to dwell at length on the proper meaning of reasonable and just as applied to the toll schedule being considered. All parties to this proceeding agree that DRPA's revenues should be sufficient to achieve a return sufficient to support its total activities, including the operation of the bridges, the PATCO rapid transit system, and the World Trade Division, and provide sufficient coverage for financings. Thus, a reasonable and just toll schedule would be one sufficient to support these activities and requirements." (Stip. 281a-282) • • •

Subsequently, after negotiations with the Federal Highway Administrator, the DRPA prepared a new toll schedule to apply as of January 1, 1974, and filed a request with the Federal Highway Administrator for a stay in order to permit the institution of the new toll schedule. (Stip. 282) • • •

On December 21, 1973, the Administrator held that it would be in the public interest to grant the DRPA's request

and ordered the proposed new toll schedule into effect. The Authority's petition stated that the impending energy crisis and other issues of public interest have produced "a serious and substantial change of circumstances since the 1972 Toll Hearing". The Administrator agreed and stated in his opinion:

> "The dimensions and scope of the present energy crisis were unforeseen at the time the evidence in the administrative record in this case was adduced. At the time the November 5 order was issued, the magnitude of the problem was only dimly perceived.
>
> "Today, the urgent need to structure toll rates for crossings in major metropolitan areas to encourage use of mass transit and carpools is more apparent and pressing." (Stip. 282-283) • • •

7. On July 1, 1974, the United States Department of Transportation submitted to the President of the Senate and to the Speaker of the House of Representatives a Study of Federal Statutes and Regulations Governing Toll Bridges, which recommended (page 10) that federal bridge acts subsequent to the 1906 statute (which are more restrictive than the 1906 act) be modified "so as to permit the imposition of bridge tolls in urbanized areas of 400,000 or more population for the purpose of achieving a more efficient use of the urban transportation system with the revenues from such tolls used for highway or transit capital improvements or transit operating assistance in the urbanized area." The study noted (page 66) that "in some areas (New York, Philadelphia, San Francisco), bridge toll revenues provide significant support for transit capital and/or operating costs, thereby providing transit service improvements which promote decreased dependence on automobile travel. Therefore, it would appear to be in the Federal interest to permit the imposition of tolls which would promote a more efficient utilization of the urban transportation system. Such a policy would not be unjustly discriminatory but more appropriately reflect the total costs of using the facility in peak demand periods." (Stip. 285) • • •

V. Urban Mass Transportation in Metropolitan New York

1. In 1970, the Governors of Connecticut, New Jersey and New York created the Governors' Special Commission on Financing Mass Transportation. The Commission rendered its report in 1972, after an 18-month study aimed at finding long-range solutions for the financing of mass transportation. In its letter of transmittal the Commission pointed out that the problem was one of finding ways of financing the comprehensive mass transportation system which would require massive subsidies if the fares were to be kept within the reach of the users. The report stated:

> "The deficit problem is huge. In the period, 1972 to 1985, the region will need $13.6 billion to finance mass transit operating deficits. This means an average of $1 billion annually will be required for operations alone. In the same period, the region will need at least $7.3 billion to finance capital outlay. The Commission believes this money can be obtained to finance the system and that the region's mass transportation problems can be solved while keeping fares within the reach of all people. . . .

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"The Mass Transit Deficit

"During The Period Covered by This study, the mass transit system experienced recurring financial crises. In response to these crises, various steps were taken to make the system more viable:

1.) existing and newly-created public authorities took over deficit-ridden operations;

2.) state and local governments and, more recently, the Federal government provided various types of financial aid;

3.) fares were increased;

4.) several unprofitable operations were discontinued.

"However, these actions could not overcome the impact of the forces that have been adversely influencing mass transit for more than a decade.

"One of the most important of these was the increasing competition of the automobile. This stemmed from growing incomes, the movement of population to the suburbs, the proliferation of suburban sites of employment, the decline of downtown shopping areas, and the deterioration of mass transit services themselves.

"During the last three years, the already poor financial situation deteriorated even further because of the influence of newly-emerging forces. Among these were:

1.) inflation generally, but more particularly the rapidly mounting cost of labor;

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2.) the downward trend in passengers on certain facilities resulting from fare increases which were expected to raise revenues by an amount greater than that actually realized;

3.) the slow-down in economic activity;

4.) the high cost of protection against crime.

"As a result the gap between passenger revenues and operating costs and debt service of the mass transit system had grown to $420 million by 1970 (Table II-1). This amount, shown in the table, represents an increase of $243 million since 1963, with more than half the increase occurring over the last two years. The size of the deficit is still rising rapidly on the basis of the data now available for fiscal 1971 and 1972.

"Mass transit operations in New York City (excluding private buses) accounted for about 85 per cent of the region's deficit. The remaining 15 per cent was mainly due to the LIRR and PATH, with New Jersey's commuter railroads accounting for about 2.5 per cent.

"In 1963 the deficit was financed almost entirely from the general funds of state and local governments, with some contributions from surpluses of public authorities and public and private bus companies. The aid from all these sources increased markedly over the last decade.

"By 1970 the deficit, even after these injections of funds, was almost $90 million. (Stip. 286-287) • • •

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"There was recourse to devices such as borrowing for current operations, postponement of payments to pension funds, and delay in payment of outstanding liabilities. Clearly, such methods of financing offer no long-run solution to the financial problems of the system."

In its letter of transmittal the Commission summarized its recommendations:

"1. The Commission recommends that each city in the region impose a mass transportation tax on all individuals who live or work in that city. Moreover, the imposition of such a tax must be contingent upon a provision whereby the Federal government will grant a 100 per cent transportation income tax credit to all individuals paying the transportation tax.

"2. The Commission recommends that the Federal government and each of the States should establish a General Transportation Fund and appropriate revenue sources should be credited to that Fund.

"3. The Commission recommends that the States should have the right to use funds received from the Federal Transportation Fund for capital outlay and/or debt service on capital outlay.

"4. The Commission recommends that the Federal share of capital projects that are part of a coordinated regional plan should be increased to 90 per cent.

"5. The Commission recommends that all three states in the region should assume responsibility for

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maintaining the rights of way of mass transportation facilities.

"6. The Commission recommends that a continuing Tri-State Mass Transportation Financing Advisory Panel should be created to study and make recommendations on problems relating to all aspects of financing public mass transportation services.

"7. The Commission recommends the transit user should pay a reasonable share of the mass transportation system's operating costs."

3. In 1967, the New York Legislature enacted Chapter 717 of the Laws of 1967, pursuant to which the Triborough Bridge and Tunnel Authority was merged into the [Metropolitan Transportation Authority] and the transfer of surplus funds of the Triborough Bridge and Tunnel Authority to the MTA and the New York City Transit Authority was authorized in order to maintain the then current New York City subway fare of 20 cents. Claiming that these surplus funds had been pledged to secure outstanding bonds of the Triborough Bridge and Tunnel Authority, the Chase Manhattan Bank, a successor trustee for the holders of $362 million of Triborough Bridge and Tunnel Authority bonds, instituted litigation seeking to prevent the transfer of the Triborough's surplus funds. The complaint of the Chase Manhattan Bank alleged in part that if the transfer of surplus funds were effected without the consent of the bondholders, the New York statute authorizing the transfer would violate the Contract clause of the Constitution of the United States. On February 9, 1968, the litigation instituted by the Chase Manhattan Bank was settled pur-

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suant to a stipulation which authorized the Triborough Bridge and Tunnel Authority to adopt an amendment to its Bond Resolutions by the vote of the holders of not less than ⅔ in principal amount of its outstanding bonds, which amendment would permit transfer of the Triborough's surplus funds to the MTA or the New York City Transit Authority and would authorize an increase in the interest rate of outstanding bonds of ¼ of 1%. The approval of the Triborough's bondholders to this amendment to its Bond Resolutions was obtained.

4. The tolls on the bridges and tunnels operated by the Triborough Bridge and Tunnel Authority subsequently were doubled. In the approximately 7 years since the merger of the Triborough Bridge and Tunnel Authority into the MTA, approximately $305 million of the Triborough's surplus funds has been paid to the MTA to reduce its deficits. There has been no default with respect to any payment to any bondholder of the Triborough Bridge and Tunnel Authority, which has not attempted to issue any further bonds since the settlement of the litigation described in paragraph 3.

5. Deficits estimated to be incurred in 1975 by the Metropolitan Transit Authority have been projected at $450 million. In September, 1974, Mayor Beame proposed that Port Authority funds be used to help reduce such deficits. This proposal prompted the adoption of the following resolution by the General Assembly of the State of New Jersey:

> "BE IT RESOLVED, that the members of the General Assembly of the State of New Jersey go on record

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> in opposition to the use of funds received from residents of New Jersey through bridge and tunnel tolls to offset operating deficits of the New York City subway and bus transit system; and,
>
> "BE IT FURTHER RESOLVED, that a copy of this resolution, signed by the Speaker and attested to by the Clerk of the New Jersey General Assembly, be sent to the Governors of New Jersey and New York, the President of the New Jersey Senate, the members of the Port Authority of New York and New Jersey, the Mayor of the City of New York, and the Chief Executive Officer of the Metropolitan Transit Authority."

6. The MTA is required to establish fares, tolls and other fees which are necessary to maintain the combined operations of the MTA and its subsidiary corporations on a self-sustaining basis.

7. The deficit nature of MTA's rail transit operations is disclosed in reports issued by its outside independent auditors. Thus, in a report dated September 28, 1973, Price Waterhouse & Co. stated that the New York City Transit Authority, which operates the New York City Subway System, received $538 million in operating revenues for its fiscal year ending June 30, 1973 and paid operating expenses of $713 million, leaving an operating deficit of approximately $175 million. This $175 million operating loss for the year ending June 30, 1973 increased the accumulated Transit Authority operating deficit to approximately $694 million. These deficits of the City Transit Authority do not include depreciation expenses, since the Authority's capital costs are borne by the City of New

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York. Approximately $165 million of the $175 million operating loss for fiscal 1973 was financed by a $73 million contribution from the Triborough Bridge and Tunnel Authority, a $75 million contribution of revenue-sharing funds by the City of New York and $17 million in other contributions by the City of New York. The total accumulated deficit after contributions by governmental sources increased from approximately $325 million in 1972 to approximately $335 million in 1973.

8. During the calendar year 1973 the MTA, as shown in reports rendered by S. D. Leidesdorf & Co. dated March 22, 1974, incurred total operating deficits on its three commuter railroads of approximately $104 million. The Long Island Railroad's net operating deficit was in excess of $77 million. That railroad received operating revenues totalling $94.7 million but paid operating expenses totalling $172.1 million and thus incurred a net operating deficit of $77.4 million. The combined operating deficits of the Harlem/Hudson Divisions of Penn Central and the New Haven Division of Penn Central amounted to approximately $27 million. However, the net operating deficit of the MTA for calendar 1973 was reported as approximately $47 million, including depreciation and similar charges of approximately $14 million. The MTA's balance sheet as at December 31, 1973, showed that the excess of its assets over its liabilities had increased to more than $398 million at the end of 1973 from approximately $357 million at the end of 1972. Adding the 1973 operating deficits of MTA's commuter railroads to those incurred by its subway system for the fiscal year ending June 30, 1973, produces a total operating deficit of $279 million. (Stip. 289-294) • • •

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VI. The Financial Position of the Port Authority

• • •

2. In the latter part of 1970, the State of New York Department of Audit and Control prepared a report (No. NY-Auth. 8-70) concerning the Port Authority . . . . The managerial summary of that report was as follows:

> "The Authority's financial condition is very strong. As of December 31, 1969, the Authority had almost $2.1 billion invested in facilities and had cash and investments of some $550 million. More than $1 billion of debt had been retired through the application of income and nearly $1.4 billion in debt was still outstanding. Each year since 1960, except for three years, more than $100 million of additional investment in facilities had been made by the Port. And in each of those three years, more than $80 million was so invested.
>
> "Net operating revenue levels experienced heretofore by the Authority appear adequate to meet existing mandatory debt repayment schedules. Furthermore, these revenues will be augmented by about $36 million a year, perhaps in 1973, when the World Trade Center becomes fully operational. We estimate that, by that time, the Authority will have sufficient resources and cash flow to support another $1 billion of bonding capacity for authorized facilities.
>
> "A further indication of the Authority's financial strength has been its ability to plow back large amounts of current operating earnings into new capital construction. During the last four years (1966

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through 1969), the Authority's net operating revenue and investment income, less interest and mandatory long term debt retirements, has averaged more than $50 million a year. During the past ten years, the Authority has accomplished $324.5 million of construction (about one-third of all its construction during that period) out of operating revenues. Generally, the Authority has done this by borrowing certain amounts on a short term basis at the beginning of each year, and repaying these borrowings before the end of the year. [The Port Authority saved itself about $252 million in interest costs by the use of this technique. (Audit Report, page 21)].

"There were a number of alternatives to the practice of plowing back earnings into new construction. For example, the moneys might have been used for other activities, additional amounts might have been provided to municipalities 'in lieu of taxes' or its rents, tolls might have been reduced, etc., but it would have been necessary to weigh the effect of the alternatives on future revenues and on long-range capital plans, and some of the alternatives would have required Executive or Legislative approval.

"The basic point is that the Authority generates substantial net revenues beyond mandatory debt service. The purposes to which these revenues are applied involves questions of public policy and priority of such importance as to warrant the attention of the Executive and Legislative branches of the two States." (Stip. 318-320) • • •

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4. The following chart compares financial information for 1973 and 1961 based upon the Port Authority's Annual Reports for those two years:

	1973	1961	% Increase
Gross Operating Revenues	$ 373,497*	$ 123,200*	203%
Net Operating Revenues	137,063	67,200	104
Net Revenue before Debt Service	160,678	71,[illegible]3	124
Net Revenue after Debt Service	84,092	37,779	123
Total Reserves	236,764	82,400	187
Bonded Debt	1,734,867	626,000	177
Invested in Facilities	3,300,000	1,116,100	196
Cumulative Debt Retired	1,261,357	538,600	134

* All $ in Thousands.

5. Port Authority reports to bondholders and the general public do not separately identify revenues, expenses or debt service of any particular facility. The Port Authority's 1962 Annual Report contained the following material from the report of outside auditors retained by the 1961 Special New Jersey Senate Investigating Committee:

> "The Authority's financial structure is based on a single enterprise, pooling of revenues concept. Individual facilities are not financed independent of the rest of the Authority. The facilities contribute their revenues for debt service according to their earning power without regard to the amount of bonds which were issued for their construction. For these

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reasons any presentation of net revenues after debt service for individual facilities is not based on actual fact. As pointed out by the Authority in submitting its report such a presentation can only be based on arbitrary assumptions.

"One thing the Authority's report does clearly indicate is that few of its facilities would have been financially feasible without the ability to pool revenues of all facilities."

6. The Port Authority does prepare internal reports showing gross revenues, operating expenses and net operating revenues or deficits for each facility and the published reports of the Authority list the amounts invested in each facility. The following chart is based upon internal Port Authority reports, except that the investment figure is taken from the latest Official Statement of the Port Authority (dated October 1, 1973):

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Facility	(In Thousands of Dollars) 1973 Grosss Revenues	1973 Operating Expenses	Net Operating Revenue (Deficit)	Investment of Port Authority as of June 30, 1973
JFK International	$125,369	$ 67,698	$ 57,671	$ 661,330
LaGuardia	42,064	26,130	15,934	172,200
Newark International	28,501	18,698	9,803	314,500
Teterboro	558	198	360	11,400
Heliports	96	500	(404)	700
Air Terminals	196,588	113,224	83,364	1,160,100
Columbia St. Marine Terminal	325	238	87	4,300
Port Newark	11,941	5,059	6,882	145,800
Erie Basin	739	740	(1)	13,000
Hoboken	873	238	635	18,100
Elizabeth	13,135	2,309	10,826	178,000
Brooklyn	5,353	2,747	2,606	95,900
Cons. Pass. Ship Terminal	2,625	3,229	(604)	2,000
Maritime Terminals	34,991	14,560	20,431	457,100
P.A. Building	4,015	2,096	1,109	23,500
N.Y. Truck Terminal	743	529	214	9,900
Newark Truck Terminal	370	368	2	8,200
P.A. Bus Terminal	11,709	9,318	2,391	60,700
Terminals	16,837	13,121	3,716	102,300
Holland Tunnel	11,754	10,637	1,117	69,300
Lincoln Tunnel	18,012	12,338	5,674	198,700
George Washington Bridge	39,894	14,385	25,509	213,200
Staten Island Bridge	15,065	7,008	8,057	64,600
Tunnels and Bridges	84,725	44,368	40,357	545,800
PATH Corporation	9,426	27,597	(18,171)	212,400
World Trade Center	30,930	23,564	7,366	707,400
Total All Facilities	373,497	236,434	137,063	3,185,100

(Stip. 321-323) • • •

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7. The following chart, showing the application of 1973 and 1961 Port Authority net revenues, was provided by the Port Authority at the request of counsel for Plaintiff:

PORT AUTHORITY OF NEW YORK AND NEW JERSEY
(in Thousands of Dollars)

	Reference	1973	1961
Net Revenue Before Debt Service	(1)	$160,678	$ 71,588
Interest on Bonded Debt	(2)	(49,729)	(14,807)
Mandatory Long-Term Debt Retirements	(3)	(26,047)	(19,002)
Interest on Bank Loans	(4)	(6,775)	—
Bank Loan Payment	(5)	(35,000)	—
Invested in Facilities	(6)	(8,000)	—
Debt Service on Bonds Secured by Trust	(7)	(6,874)	—
Adjustment of Securities Value	(8)	(3,591)	(1,943)
Short-Term Note Maturities			(32,000)
Debt Retirement and Acceleration			(489)
Net Increase in Reserves	(9)	$ 24,662	$ 3,347
Reserves from Prior Years in Excess of Amount of Next Two Years' Bonded Debt Service	(10)	3,675	1,625
Available to Satisfy Reserve Requirements	(11)	28,337	4,972
Applied to Bring:			
General Reserve Fund to 10% of Bonded Debt	(12)	16,806	1,527
Total Reserves to Amount of the Next Two Years' Bonded Debt Service	(13)	7,793	2,424
Sub Total		$ 24,599	$ 3,951

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	Reference	1973	1961
Reserves at Year End in Excess of Next Two Years' (1974-1975) Bonded Debt Service—Held to Meet Obligations in the Following or Subsequent Years	(14)	$ 3,738	$ 1,020

NOTE: 1961 Amounts May Not Add Due to Rounding.

REFERENCES

1. 1973 Annual Report, Statement A, Line 6. The amount shown does not take into account adjustment of securities value.
2. 1973 Annual Report, Statement A, Line 7.
3. 1973 Annual Report, Statement A, Line 7.
4. 1973 Annual Report, Statement A, Line 8.
5. 1973 Annual Report, Statement A, Line 9.
6. 1973 Annual Report, Statement A, Line 11.
7. 1973 Annual Report, Statement I, Line 18.
8. 1973 Annual Report, Statement A, Line 15.
9. 1973 Annual Report, Statement A, Line 14.
10. The amount shown for 1973 was calculated by sub tracting from the Total Reserve Balances at the end of 1972 ($212,102) the total Debt Service for 1973 and 1974 ($208,427).
11. Sum of (9) and (10).
12. The General Reserve Fund was established in 1931 by legislation adopted by the States of New Jersey and New York. Under this legislation, the Port Authority

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maintains the General Reserve Fund at 10% of the par value of all outstanding bonds secured by that Fund, including Consolidated Bonds, which were issued in order to raise moneys to finance or refinance Port Authority facilities.

13. See paragraph 9 for an explanation of this item.

14. The Bonded Debt Service for the next two years equals $233,026.

8. The following chart shows the total reserves of the Port Authority as of December 31, 1973:

Amounts required in 1974 and 1975 for interest and amortization of bonded debt	$233,026,000
Reserves at year end 1973 in excess of 1974 and 1975 bonded debt interest and amortization	3,738,000
Total reserves as of December 31, 1973	$236,764,000

9. As noted in Reference 12 to the chart in paragraph 7 above, the Port Authority maintains the General Reserve Fund at 10% of the par value of all outstanding bonds secured by that Fund including Consolidated Bonds, which were issued in order to raise moneys to finance or refinance Port Authority facilities. In addition, it has been the Port Authority's consistent practice since 1948 to maintain in reserve an amount equal to the next two years bonded debt service, which includes interest and amortization. This practice has been publicly disclosed in the Port Authority's Annual Statements (see page 58 of the 1961 Annual Report, page 68 of the 1962 Annual Report and page 58 of the 1973

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Annual Report) and was discussed by Dwight R. G. Palmer, New Jersey State Highway Commissioner, in his testimony before the Farley Committee. Mr. Palmer stated that the maintenance of this policy "strengthened [the Port Authority's] credit position" and "such reserves [the two year debt and General Reserve Fund] cannot be regarded as uncommitted funds". According to the 1971 Annual Report of the Port Authority, the Bonded Debt requirements for 1972 and 1973 totalled $189,028,000. According to the 1973 Annual Report, revenues in 1972 and 1973 were charged with a total of $152,124,000. The balance of the debt service was attributable to construction in progress and capitalized by the Port Authority.

VII. Port Authority Bonds

1. From 1969 through the end of 1973, the Port Authority obtained the funds necessary for construction of its various projects from the following sources: long-term debt (Consolidated Bonds)—$700 million; medium-term debt (6 or 7 year bank loans)—$260 million; short-term debt (1-year notes)—$290 million, all but $15 million of which was refunded in medium or long-term debt; appropriations from reserves—$61 million. The Port Authority has not issued Consolidated Bonds since October 1973, although it has continued construction work on its various projects. (Stip. 324-327) • • •

3. On October 9, 1952, the Port Authority adopted a Consolidated Bond Resolution, authorizing and establishing an issue of Consolidated Bonds "to serve as a unified medium for financing for any and all purposes for which

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the Authority is or shall be authorized to issue bonds secured by a pledge of the General Reserve Fund." The text of this resolution appears as Appendix V to the Official Statement (Exhibit II) issued in October 1973 with respect to the Forty-first Series of Consolidated Bonds, the most recent series of such bonds. Section 3 of the Consolidated Bond Resolution of October 9, 1952 prohibits the issuance of new Consolidated Bonds unless the one year net revenues of all of the Port Authority's facilities amount to 1.3 times the prospective debt service for the calendar year during which the debt service of all outstanding and proposed new bonds secured by a pledge of the General Reserve Fund would be at a maximum. Section 4 of the October 9, 1952 Consolidated Bond Resolution provided that the net revenues of all Port Authority facilities were pledged to the payment of the debt service of Consolidated Bonds subject to the pledges and liens existing with respect to the General and Refunding Bonds, Air Terminal Bonds and Marine Terminal Bonds. Section 6 of the October 9, 1952 Consolidated Bond Resolution provided that the payment of debt service upon all Consolidated Bonds "shall be further secured equally and ratably by the General Reserve Fund." Moneys in the General Reserve Fund were not to be used for any purpose if there were other moneys of the Port Authority available for that purpose, unless there were sufficient funds available to the General Reserve Fund to pay debt service upon outstanding bonds during the ensuing 24 months, in which event such excess moneys could be used for any purpose permissible under the General Reserve Fund statutes, whether or not other moneys were available for that purpose. Section 7 of the October 9, 1952 Consolidated Bond Resolution established

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a Consolidated Bond Reserve Fund into which all net revenues pledged as security for Consolidated Bonds (after payment of debt service on all Consolidated Bonds and of amounts necessary to bring the General Reserve Fund to its statutory level) were required to be paid. The moneys of the Consolidated Bond Reserve Fund could be used only for the payment of: Consolidated Bonds at maturity, retirement or redemption; debt service upon outstanding Consolidated Bonds; the deficit of any facility the net revenues of which were pledged as security for Consolidated Bonds; and "any other additional purposes for which the Authority is now or may hereafter be authorized by law to expend the revenues of its facilities." (Stip. 327-329) • • •

5. Outstanding Consolidated Bonds as of December 31, 1973 were as follows:

Series	Interest and Maturity	December 31, 1973 (000 Omitted)
First Series	3% due 1982	14,077
Second Series	2¾% due 1984	14,960
Fourth Series	2¾% due 1985	21,000
Fifth Series	2.90% due 1983	12,300
Sixth Series	3% due 1986	19,800
Seventh Series	3.40% due 1986	16,900
Eighth Series	3.40% due 1987	35,000
Ninth Series	3½% due 1973-1975	2,700
Tenth Series	3¾% due 1985	24,000
Eleventh Series	3% due 1973-1978	10,000
Twelfth Series	3⅜% due 1988	30,030
Thirteenth Series	Various due 1973-1978	6,250
Fourteenth Series	3⅝% due 1989	42,845

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Series	Interest and Maturity	December 31, 1973 (000 Omitted)
Fifteenth Series	Various due 1973-1979	10,500
Sixteenth Series	4¼% due 1989	19,475
Seventeenth Series	Various due 1973-1980	10,500
Eighteenth Series	Various due 1973-1981	16,450
Nineteenth Series	3½% due 1991	20,500
Twentieth Series	3¼% due 1993	31,500
Twenty-First Series	3.40% due 1993	22,500
Twenty-Second Series	3⅜% due 1993	22,500
Twenty-Third Series	3⅜% due 1994	23,000
Twenty-Fourth Series	3½% due 1994	23,000
Twenty-Fifth Series	Various due 1973-1984	16,500
Twenty-Sixth Series	3½% due 1995	33,250
Twenty-Seventh Series	3⅜% due 1995	24,500
Twenty-Eight Series	3⅜% due 1996	24,625
Twenty-Ninth Series	3½% due 1996	24,625
Thirtieth Series	3⅝% due 1998	24,500
Thirty-First Series	4% due 2002	99,500
Thirty-Second Series	5% due 2003	100,000
Thirty-Third Series	4¾% due 2003	100,000
Thirty-Fourth Series	5½% due 2003	100,000
Thirty-Fifth Series	6⅝% due 2005	100,000
Thirty-Sixth Series	6.40% due 2005	50,000
Thirty-Seventh Series	6% due 2006	100,000
Thirty-Eighth Series	5⅜% due 2006	100,000
Thirty-Ninth Series	5.80% due 2007	150,000
Fortieth Series	6% due 2008	100,000
Forty-First Series	5½% due 2008	100,000
		$1,697,286

(Stip. 329-330) * * *

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6. * * * The following language appeared in each Official Statement as distributed in connection with the sale of Consolidated Bonds from the time of adoption of the covenant through the Thirty-ninth Series Statement:

> "In connection with the legislation which authorized the Port Authority to assume responsibility for the Hudson Tubes system, the Port Authority had advised the Legislatures of both States that the credit of the Port Authority would be impaired by such an undertaking of an anticipated perpetual deficit facility unless the States would enter into an enforceable contract with the Port Authority bondholders which would grant assurances against dilution of already pledged revenues and reserves by any additional passenger rail deficits beyond those of the basic Hudson Tubes system. The legislation as finally adopted includes such statutory covenants. The covenants are between the two States and with the holders of certain described "affected" bonds which include all Consolidated Bonds including those of the present offering. The contract prohibits the application of any revenues or reserves pledged to such bonds (which includes all existing revenues, other than rentals under the New York State's Commuter Railroad Car Program described on pp. 18-19, and all existing reserves) for any additional passenger railroad purpose beyond the basic Hudson Tubes, as defined, without the consent of the holders of such affected bonds as provided in their contract with the Authority unless the Port Authority shall have first certified the eligibility of such additional railroad, whether it be a Hudson Tubes extension, as defined,

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or new railroad facility. To be eligible the Port Authority must determine either that the proposed additional passenger railroad facility is self-supporting or, if not, that at the end of the preceding calendar year the General Reserve Fund contained the full statutory amount and that for the ensuing ten years the estimated average annual deficits from the proposed additional passenger railroad facility and any then existing Port Authority passenger railroad facility (including the basic Hudson Tubes) would not in the aggregate exceed an amount equal to one-tenth of the amount in the General Reserve Fund at the prior year end. Certain adjustments to this figure are provided by the statute. For example, the amount equal to one-tenth of the General Reserve Fund is to be diminished by an amount equal to 1% of the principal amount of Port Authority bonds the proceeds of which shall have been applied for passenger railroad purposes; this prevents the enlargement of deficit capacity by bonds issued in connection with a deficit passenger railroad facility. Furthermore, if at some time in the future the adjusted 10% of the General Reserve Fund should be exceeded by an amount equal to 1% of the Port Authority's equity, as defined in the statutes, augmented by 1/10 of that adjusted 10%, then the augmented 1% of equity may be used as the limiting figure instead of the percentage of the General Reserve Fund. Also, the limiting figure may be enlarged to the extent of State subsidies for passenger railroad purposes. Section 6 of the 1962 legislation (see Appendix III) should be studied for the exact terms of the statutory covenant."

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The Fortieth and Forty-first Series Official Statements noted that the above statement *"does not apply to bonds of the present offering"* and also included the following language:

> "The statutory covenant against dilution of pledged revenues and reserves by additional passenger railroad facilities, which is discussed in the paragraph quoted above, remains in effect with respect to affected bonds, and remains binding on the Authority although it does not apply to the bonds of the present offering. The legislation which authorized the Port Authority to assume responsibility for the Hudson Tubes system was amended, effective May 10, 1973, by the States of New York and New Jersey (Ch. 1003, Laws of New York 1972, Ch. 318, Laws of New York 1973; Ch. 208, Laws of New Jersey 1972). The New Jersey amendment, when introduced in the New Jersey Assembly, was accompanied by a statement that the bill was intended to preclude the application of the covenant to holders of bonds newly issued after its effective date, while maintaining in status quo the rights of the holders of the bonds issued after March 27, 1962 (the effective date of the covenant legislation) but prior to the effective date of the amendment."

"In a report to the Port Authority, dated December 8, 1971, The First Boston Corporation stated:

'We have been advised by our counsel Mudge Rose Guthrie & Alexander, that the '1962 Covenant' is legally binding. This covenant prohibits the application of Port Authority moneys for any 'railroad

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purposes' other than 'permitted purposes'; these 'permitted purposes' do not encompass additional passenger rail transportation projects except insofar as they are self-supporting or incur an aggregate annual deficit of less than 10% of the Port Authority's General Reserve Fund (which limitation, based on Port Authority reports, has already been exceeded by the Path operation). This precludes general credit financing of any passenger transportation project, no matter how desirable, for which projections show an operating profit below debt service requirements.

"The First Boston Corporation further stated that it considered:

'the financing (through the medium of Consolidated Bonds) of certain peripheral railroad facilities as 'adjuncts', that is, as projects which are integral to airport operation, and which serve the airport only, not commuters generally. However, such 'adjuncts' would need the benefit of a conclusive legal holding to the effect that they constitute part of an existing facility; presumably the nature of the 'adjunct' would determine the distance outside the airport boundaries that it might extend and still be legally treated as an 'adjunct' for financial purposes.'

"Should this 'adjunct' theory prevail with respect to the rail access projects to John F. Kennedy and Newark International Airports, and should the projects be authorized on such basis, it would be unnecessary for the Port Authority to certify the projects as self-supporting under the 1962 statutory covenant described above." (Stip. 330-333) • • •

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7. The Port Authority has stated in the Official Statements covering the issuance of its Consolidated Bonds (for example, page 22 of the Official Statement for the Forty-first Series of Consolidated Bonds):

> "it is the present intention of the Authority that Consolidated Bonds will be the only bonds secured by a pledge of the General Reserve Fund that will be used as a medium of financing the balance of its capital requirements or long-term refunding of outstanding bonds or of Consolidated Bonds hereafter issued."

8. Section 7 of the resolutions establishing each series of Consolidated Bonds prohibits the issuance of any Consolidated Bonds or other bonds to be secured by a pledge of the General Reserve Fund with respect to any facility or group of facilities with respect to which the Authority has not previously issued bonds unless:

> "the Authority shall certify at the time of issuance its opinion that the issuance of such Consolidated Bonds or that such pledge of the General Reserve Fund as security for such bonds other than Consolidated Bonds will not, during the ensuing ten years or during the longest term of any of such bonds proposed to be issued (whether or not Consolidated Bonds), whichever shall be longer, in the light of its estimated expenditures in connection with such additional facility or such group of additional facilities, materially impair the sound credit standing of the Authority to fulfill its commitments, whether statutory or contractual or reasonably incidental thereto, including its undertakings to the holders of Consolidated Bonds." (Stip. 336) • • •

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11. The two principal bond rating agencies, Moody's and Standard & Poor's, have commented on the 1962 Covenant and the effects of its elimination. The Moody's Report dated October 5, 1973, rating the Bonds in connection with the imminent sale of the Forty-first Series, stated in part:

"Rating: Consolidated Bonds: A

"Summary: Despite the clouded future surrounding the World Trade Center and the role, if any, which Port Authority will play in a regional mass transportation system, the Authority's financial position remains strong. Financial strength continues to accrue from the Authority's monopoly on Hudson River crossings and operations at the three important commercial airports in the New York metropolitan area.

"Although bonds of this and the previous issue are not subject to the 1962 statutory covenant barring application of Authority funds to additional deficit passenger railroad operations, the covenant remains in effect as long as any bonds issued under the legislation remain outstanding. As of December 31, 1972 the Authority had outstanding $1,175,500,000 from 20 series of Consolidated bonds issued under the covenant, the last of which is due in 2007. A suit now in the Supreme Court of New York State seeks to permit unlimited application of surplus Authority funds to deficit passenger railroads. If the suit is successful, demands for mass transportation would probably obstruct further Authority expansion into other fields. Bondholder protection would remain

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adequate because debt service constitutes a first lien on net revenues.

• • •

"Structure: This issue of Consolidated Bonds is due in 2008. . . .

• • •

"Mass Transportation: All Authority bonds issued between March 27, 1962 and May 10, 1973 are subject to a statutory covenant against dilution of revenues pledged to the bonds. The legislation prohibits application of all revenues (other than rentals under the New York State commuter railroad car program) and all reserve for any additional passenger railroad purpose beyond the basic Hudson Tubes without consent of bondholders unless the Authority certifies 1) that the proposed facility will be self-supporting, including grants from governments, or 2) that the General Reserve contained the required amount at prior year-end, and that annual deficits from existing and proposed passenger rail facilities would not exceed 1/10 of the amount in the General Reserve Fund at the prior year-end. Although it does not apply to bonds of the Fourtieth and Forty-First Series, the restrictive covenant remains in effect as long as any bonds issued under that legislation are outstanding. As of December 31, 1972 the Authority had outstanding $1,175,500,000 from 20 series of Consolidated bonds issued under this covenant. The final issue under this legislation was the Thirty-ninth Series, which is due in the year 2007.

"The statutes which authorize rail access to Kennedy International Airport and Newark Interna-

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tional Airport revised the definition of 'air terminals' to include mass transportation facilities between the air terminals and other points in the Port District. Hawkins, Delafield & Wood, Bond Counsel for the Authority, is of the opinion that unless such a project were to meet the requirements against dilution of pledged revenues, any financing of such a project by the Authority would be violation of the statutory covenant.

"A suit currently in the New York State Supreme Court, challenges the constitutionality of the statutory covenant and seeks to permit unlimited application of surplus Authority funds to deficit passenger rail operations. If the suit is successful, the demands for mass transportation would probably obstruct further Authority expansion into other fields. Bondholder protection would remain adequate, because debt service constitutes a first lien on net revenues.

"Legislation in 1962 authorized the Authority to undertake a project consisting of a World Trade Center and the Hudson Tubes. The Authority estimated that operations of the Hudson Tubes, including debt service and depreciation, will involve an increasing annual deficit of more than $20 million. Depreciation, which in recent years has been excluded from public-transit-system accounting, was estimated by the Authority at $6 million in 1972.

"In June 1973 Port Authority Commissioners from New York and New Jersey approved and PATH (Port Authority Trans-Hudson Corp.) adopted a

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fare increase from 30¢ to 50¢, but the Interstate Commerce Commission would not grant the increase without further hearings, which were scheduled to begin September 24, 1973. On September 21, 1973 the New York Commissioners, led by Governor Rockefeller, suggested that the fare increase be increased to only 35¢. On September 24, 1973 the hearings were closed after PATH requested an adjournment. On September 28, 1973 PATH filed a petition to reopen the hearings on the fare increase as adopted in June."

The Moody's Report dated October 15, 1973 stated in part:

"Summary: Despite the clouded future surrounding the World Trade Center and the role, if any, which Port Authority will play in a regional mass transportation system, the Authority's financial position remains strong. Financial strength continues to accrue from the Authority's monopoly on Hudson River crossings and operations at the three important commercial airports in the New York metropolitan area.

"Although the two series of Consolidated bonds issued in 1973 are not subject to the 1962 statutory covenant barring application of Authority funds to additional deficit passenger railroad operations, the covenant remains in effect as long as any bonds issued under the legislation remain outstanding. As of December 31, 1972 the Authority had outstanding $1,175,500,000 from 20 series of Consolidated bonds issued under the covenant, the last of which

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is due in 2007. A suit now in the Supreme Court of New York State seeks to permit unlimited application of surplus Authority funds to deficit passenger railroads. If the suit is successful, demands for mass transportation would probably obstruct further Authority expansion into other fields. Bondholder protection would remain adequate, because debt service constitutes a first lien on net revenues.

"Hudson Tubes Facility: The Authority estimates that operations of the Hudson Tubes, including debt service and depreciation, will involve an increasing annual deficit of more than $20 million. Depreciation, which in recent years has been excluded from public-transit-system accounting, was estimated by the Authority at $6 million in 1972.

"In June 1973 Port Authority Commissioners from New York and New Jersey approved and PATH (Port Authority Trans-Hudson Corp.) adopted a fare increase from 30¢ to 50¢, but the Interstate Commerce Commission would not grant the increase without further hearings, which were scheduled to begin September 24, 1973. On September 21, 1973, the New York Commissioners, led by Governor Rockefeller, suggested that the fare be increased to only 35¢. On September 24, 1973 the hearings were closed after PATH requested an adjournment. On September 28, 1973 PATH filed a petition to reopen the hearings on the fare increase as adopted in June. The petition seeking a fare increase to 50¢ was rejected by the ICC on October 10, 1973, and a request for further hearings on the subject was denied.

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"Additional Passenger Railroad Facilities: All Authority bonds issued between March 27, 1962 and May 10, 1973 are subject to a statutory covenant against dilution of revenues pledged to the bonds. The legislation prohibits application of all revenues (other than rentals under the New York State commuter railroad car program) and all reserves for any additional passenger railroad purpose beyond the basic Hudson Tubes without consent of bondholders unless the Authority certifies 1) that the proposed facility will be self-supporting, including grants from governments, or 2) that the General Reserve contained the required amount at prior year-end, and that annual deficits from existing and proposed passenger rail facilities would not exceed 1/10 of the amount in the General Reserve Fund at the prior year-end. Although it does not apply to bonds of the Fortieth and Forty-first Series, the restrictive covenant remains in effect as long as any bonds issued under that legislation are outstanding. As of December 31, 1972 the Authority had outstanding $1,175,500,000 from 20 series of Consolidated bonds issued under this covenant. The final issue under this legislation was the Thirty-ninth Series, which is due in the year 2007.

"The statutes which authorize rail access to Kennedy International Airport and Newark International Airport revised the definition of 'air terminals' to include mass transportation facilities between the air terminals and other points in the Port District. Hawkins, Delafield & Wood, Bond Counsel for the Authority, is of the opinion that unless such a proj-

ect were to meet the requirements against dilution of pledged revenues, any financing of such a project by the Authority would be violation of the statutory covenant.

"A suit currently in the New York State Supreme Court, challenges the constitutionality of the statutory covenant and seeks to permit unlimited application of surplus Authority funds to deficit passenger rail operations. If the suit is successful, the demands for mass transportation would probably obstruct further Authority expansion into other fields. Bondholder protection would remain adequate, because debt service constitutes a first lien on net revenues.

"The proposal for additional passenger railroad facilities was intended to provide for 1) PATH rail link connecting Newark International Airport and Penn Station in Newark 2) extension of PATH into Union County to Plainfield via Newark International Airport 3) direct rail service to Penn Station in Manhattan for Erie Lackawanna riders including equipment yard in Secaucus and a new Hackensack River Bridge. Total capital costs were estimated at $650 million. The Authority has stated that the project could be effectuated on a self-supporting basis if governmental funds of $400 million were contributed to construction funds."

"Operations: Operating data for 1972 show moderate increases in traffic on the Authority's toll bridges and tunnels, a small increase in plane movements with a substantial rise in airport passengers

(due to use of larger planes with greater capacities), and large increases in ship arrivals and waterborne cargo. Marine terminal operations reflect recovery from the East Coast dock strike in 1971. Financial operations improved considerably in 1972. Net revenues rose 12.4% compared to a decrease of 1.2% in 1971. Gross operating revenue rose 14.2% compared to 9.6% in 1971. Operating and maintenance expenses grew only 13.6%, down substantially from the 20.9% growth rate in 1971, and in line with growth in revenues."

The Moody's Report dated November 1, 1973 stated in part:

"ADDENDUM

"Our sale report and review report on this unit, dated October 5, 1973 and October 15, 1973 respectively, cited a suit filed in the Supreme Court of New York State, challenging the constitutionality of 1962 legislation which prohibits application of virtually all Authority revenues and reserves to any additional deficit passenger railroad operations beyond the basic Hudson Tubes. It should be noted that if the 1962 legislation is held to be unconstitutional, Authority funds will not *automatically* become available for additional passenger railways. Such a procedure can only be established through bi-state legislation."

The Standard & Poor's Report dated June 16, 1973, rating the Bonds in connection with the imminent sale of the Fortieth Series, stated in part:

"$100,000,000 Bonds Rated A"

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"The Authority covenants to establish charges in connection with its facilities so that the net revenues pledged to the Consolidated Bonds or the surplus revenues from those facilities which are payable into the General Reserve Fund will be at least sufficient to provide for debt service on Consolidated Bonds. Additional parity bonds may be issued if, in general, net revenues for any 12 consecutive months out of the previous 36 months, adjusted to reflect estimated net revenues (not exceeding 25% of the 12 months' historical net revenues) to be derived from uncompleted or recently completed facilities, are equal to 1.3 times maximum annual debt service on all Consolidated Bonds to be outstanding. It is also required (by Section 7 of the Fortieth Series bond resolution, as well as by previous Series' resolutions) that the Port Authority, relative to the financing of any additional facility for the first time by Consolidated Bonds or other bonds sharing in the pledge of the General Reserve Fund, must first certify its opinion that such issuances will not thereby, during the ensuing ten years or during the longest term of the bonds, proposed to be issued, whichever would be longer, materially impair the sound credit standing of the Authority or the investment status of Consolidated Bonds or the ability of the Authority to fulfill its commitments, including its undertaking to the holders of Consolidated Bonds.

"The 1962 legislation authorizing the Port Authority to acquire the Hudson Tubes and construct the World Trade Center contained a statutory covenant limiting the Port Authority's financial participation

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in additional deficit railroad facilities beyond those of the Hudson Tubes. In essence, the 1962 covenant prohibits the application of any revenues or reserves pledged to Consolidated Bonds for any additional passenger railroad purposes beyond the basic Hudson Tubes without bondholder approval unless the Port Authority and the Governors of New York and New Jersey shall certify that the proposed additional passenger railroad facility is self-supporting or, if not, that the General Reserve Fund contains its full statutory amount and that for the ensuing ten years the estimated average annual deficits from the proposed additional passenger Railroad facility and any then existing Port Authority passenger railroad facility (including the basic Hudson Tubes) would not in the aggregate exceed an amount equal to 1/10 of the amount in the General Reserve Fund at the prior year end. Certain adjustments are provided by the statute: the amount equal to 1/10 of the General Reserve Fund is to be diminished by an amount equal to 1% of Port Authority bonds the proceeds of which shall have been applied for passenger railroad purposes. This certification relates only to the Port Authority's own investment in the particular facility.

"Considerable controversy has surrounded the Port Authority's involvement in mass transit, and, in particular, the 1962 Covenant outlined above. Since the PATH deficit has been growing steadily and currently is estimated to be in excess of $20-million annually, there is obviously no room within the 1962 Covenant restrictions for the Authority to

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take on additional deficit rail transit operations. During 1971-73 several amendments to earlier statutes, including the 1962 legislation, were passed by the Legislatures of New York and New Jersey. These amendments authorized the Authority to provide mass transportation facilities connecting with Kennedy and Newark Airports: to extend the Hudson Tubes from Newark to Plainfield, and to undertake a series of New Jersey rail improvements with respect to direct Erie-Lackawanna and Penn Central railroad service into Pennsylvania Station in New York City; and provided that the provisions of the 1962 Covenant which limits the Port Authority's financial participation in additional deficit railroad facilities shall not apply to Port Authority obligations issued after May 10, 1973. Thus, the 1962 Covenant remains in effect with respect to all bonds previously issued (which have a maximum maturity in 2007) and remains binding on the Authority so long as those bonds remain outstanding. From a practical point of view, all Consolidated Bonds, including the present Fortieth Series, will continue to enjoy the protection of the 1962 Covenant until all bonds issued prior to May 10, 1973, shall have been retired.

"The legislation authorizing rail access to Kennedy and Newark airports amended the definition of 'air terminals' to provide that: 'It shall mean facilities providing access to an air terminal, consisting of rail, rapid transit or other forms of mass transportation. . . .' There appears to be some question as to the legal necessity for the Port

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Authority to certify these particular projects as self-supporting. However, in connection with the present Fortieth Series Bonds, the Port Authority states: 'It is presently intended that passenger railroad facilities authorized by that legislation be effectuated on a self-supporting basis, including substantial amounts of governmental financial aid. Additional railroad facilities which meet the test of self-support would be permitted purposes under the 1962 covenant legislation.'

"The Port Authority has experienced a steady record of increasing operating revenues over the years, gross operating revenues growing from $154-million in 1963 to $320-million in 1972. With the exception of 1971, when there was a slight decline, net revenues available for debt service have shown a similar strong growth, increasing from $79-million in 1963 to $140-million in 1972. In all years interest and mandatory long term debt retirements have been covered in excess of two times by available net revenues. The $140-million available net revenues for 1972 would cover estimated maximum annual debt service ($112,478,000 in 1986) on all Consolidated Bonds to be outstanding 1.25 times. Debt service declines sharply thereafter. The improvement in net revenues from $125-million in 1971 to $140-million in 1972 was the largest in at least the last ten years and has been obtained despite an increasing annual PATH operating deficit. Significant additional revenues could undoubtedly be produced, if needed, through modest increases in tolls and other charges for use of Port Authority facilities.

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"Despite efforts to involve the Port Authority more deeply in mass transit, and despite statements relative to the Authority's participation of $250-$300 million out of a total of $650-million Federal, State and Authority funds for the recently authorized rail transit improvements, it is apparent that present legislation does not permit such employment of Authority funds without safeguards. It appears that present legislation does not open a 'Pandora's box' of unknown adventures in the field of deficit mass transit operations, but does, in practice, continue to provide support for the credit standing of the Port Authority's bonds by restricting the extent to which the Port Authority can become involved with deficit rail facilities. Undoubtedly, future efforts will be made to 'tap-the-till' of the Port Authority to finance mass transit facilities in the New York metropolitan area, and such efforts should be carefully watched as to their potential impact upon the quality of the revenues pledged to service the Authority's bonds. It should be recognized that the ability of the Port Authority to accomplish what it has in the development of facilities vital to the metropolitan New York and New Jersey region has been in great measure dependent upon the Authority's ability to borrow the required capital funds. Such ability to borrow at favorable interest rates depends upon the Authority's credit standing in the financial community and efforts which would diminish this credit standing, such as the move in 1972 by the New York legislature to retroactively repeal the 1962 Covenant, should be carefully weighed by all concerned.

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"In the meantime, we are continuing our 'A' rating on the Port Authority's Consolidated Bonds, including the present Fortieth Series, based upon the Authority's strong operating, financial and management record, the prospects for a continuation of this record, and the protection afforded by current legislation from unforeseen dilution of pledged revenues and reserves by unrestricted involvement in deficit mass transit operations."

The October 6, 1973 Standard & Poor's Report stated: "On October 9th. THE PORT AUTHORITY OF NEW YORK AND NEW JERSEY plans to sell at competitive bidding $100,000,000 Consolidated Bonds, Forty-first Series, Due 2008 (First Installment). The bonds will be secured equally and ratably with outstanding Consolidated Bonds. On June 20, 1973, the Port Authority sold $100,000,000 Consolidated Bonds, Fortieth Series, which was discussed at length in the Fixed Income Investor of June 16, 1973, beginning on page 754. We are maintaining our 'A' rating."

12. On April 30, 1974 Governor Byrne of New Jersey signed into law an Act of the New Jersey Legislature (1974 Laws of New Jersey Ch. 25) repealing Section 3 of the 1972 law, quoted at page 256. Concurring legislation was signed into law by Governor Wilson of New York on June 15, 1974 (1974 Laws of New York Ch. 993).* The New York Legislation prompted the following discussion:

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* The bill was introduced on February 15, 1974. The repealing legislation was enacted by both States without amendment, legislative fact-finding at the 1974 Session, extensive contemporary legislative debate, public hearing or committee reports. Part III of this Stipulation discusses the legislative history of the enactment of the 1962 Covenant and of the proposals in 1971, 1972 and 1973 to repeal the Covenant.

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"THE CLERK: Senate Bill 10607, Rules Report No. 364, Caemmerer. An Act to repeal section two of chapter one thousand three of the laws of nineteen hundred seventy-two, entitled 'An Act to amend chapter two hundred nine of the laws of nineteen hundred sixty-two, entitled "An Act to provide for the financing and effectuation by the port of New York authority of a port development project, consisting of the Hudson tubes, the Hudson tubes extensions and a world trade center, for coordinating, facilitating and promoting the transportation of persons and the flow and exchange of trade and commerce in and through the port of New York district, and agreeing with the state of New Jersey with respect thereto", in relation to the application of rentals, tolls, fares, fees, charges, revenues or reserves of the port authority,' relating to the application of certain changes effected thereby."

"MR. KOPPELL: Mr. Speaker, this is a piece of legislation which has been discussed on this floor in various forms for three years, now, and with the passage by this House and hopefully the signature of the Governor, the State of New York and New Jersey will have repealed a covenant which has prevented the use of any Port Authority funds for rail mass transportation purposes in the Port Authority district which embraces the state or portions of the state of New York and New Jersey. I and many others have been fighting since 1971 to see that these covenants are taken out of the Bond Issues to which they are addressed. I want to make clear to this House and to the record a number of things, and for

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that purpose I would like to address questions to Mr. Farrel who is the sponsor in this House. Would Mr. Farrell yield?"

"ACTING SPEAKING FIELD: The gentlemen yields."

"MR. KOPPELL: Mr. Farrell, I am right I presume, and we can say for the record, can we not, that this House is passing this legislation today because of urgent need for additional funds for mass transportation purposes, rail transportation purposes, in the Port Authority district?"

"MR. FARRELL: That is correct, Ollie."

"MR. KOPPELL: And, George, is it not also true that because of the fact that the 1972 Bond Issue was not approved by the people and because the state has already extended itself in providing over $100 million to mass transportation that it is unlikely that at this time we can see a further contribution or at least a further major contribution of mass transportation from any other source than the Port Authority?"

"MR. FARRELL: Well, Ollie, that is correct. As you know, we have already approved in this session a much more modified mass transit bond issue in the sum of $250 million which will be presented to the people this November,* and we all recognize that although hopefully if it is approved it will certainly be a great stimulus in terms of capital improvement

* This bond issue was adopted by the voters of New York in November, 1974 [footnote added by stipulation].

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and development with respect to mass transit, there is no question but that the overall demands of the state areas with respect to mass transportation would never be satisfied out of that Bond Issue. As a result, the ability of the Port Authority to become more intimately involved, to become more directly involved and more quickly involved in mass transit would serve to assist us with respect to on-going programs that we have in New York, that are still to be completed out of the 1967 Bond Issue although those monies have all been committed to specific projects, and also to allow our existing systems operated under M.T.A., to be concerned with those facilities that presently exist with the Port Authority, hopefully development of lines between Penn Station and Kennedy Airport. The passage of this legislation—as you know it has already passed both Houses of the Jersey Legislature and has been signed by Governor Byrne—passage of this legislation and the approval of it by the Governor could put us directly on the road towards a greater development of mass transit in the metropolitan area of New York-New Jersey."

"MR. KOPPELL: And I agree with that, George, and would you not also say that whatever the judgment of the 1961 and 1962 Legislature may have been, it is the judgment of this Legislature that Port Authority must play a role in the development you spoke of?"

"MR. FARRELL: Yes. Well, Ollie, I think it is safer to assume although neither one of us who were here

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—as a matter of fact there are very few members who are here right now who were present in this Chamber in 1962—but at that time the urgency of mass transportation in terms of the total complexion of problems relating to transportation, had not peaked to the point that it has today in 1974, and as a result it may have been the sense of the Legislatures of New Jersey and New York at that time, but there wasn't the type of urgency that exists as it does today in 1974, and so basically what we are saying is that we are not being critical of the 1962 Legislatures of New York and New Jersey for what they have done but we are trying to say to the people and to the courts and to the bond holders and to all of us who are concerned about the bi-state area that today, 1974, mass transit must be the most important factor in the overall problem of transportation and not rubber and not concrete, and for that reason I think that what we are doing is consonant with everything else that we have done with the 1967 Bond Issue which addressed itself to the first bond sold directly to mass transportation, to the attempt that was made in 1973 for approval of the people for another bond issue in that area, and here again in 1974 with the presentation to the people of another bond issue in the amount of $250 million the establishment for the first time in the history of this state of a real preservation act which goes to the problem of abandoned railroads in upstate New York particularly, and revitalization of freight service, that we are in a new era. The Legislature has addressed itself to that era and this is just one

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further step in addressing ourselves to a very critical problem in the hopes that monies that are available to the Port Authority can be funneled in that direction."

"MR. KOPPELL: One last question, George. You would agree I take it with Governor Rockefeller's assessment that this step of repealing these so-called covenants will not affect the security of the bond holders in their investment nor impair the ability of the Port Authority to pay when they are due installments of interest and principal."

"MR. FARRELL: Well, let me just say this, Ollie, that I don't preceive of a situation occurring in which any one holding a Port Authority Bond because of the backing that the Port Authority has received from both states, the State of New York and New Jersey, they should feel in any sense of the term that the responsibility for the payment of those bonds is in jeopardy. However, I must say to you in all fairness, Ollie, because there have been statements made by Governor Wilson, not in opposition to what we are doing here today but simply to point out something which in his mind poses a potential problem. I must say to you, Ollie, that, ladies and gentlemen of the House, that this is not something that Governor Wilson has an opinion and for which no one else shares in that opinion and concern. The concern has been expressed presently and in the past by Comptroller Levitt, and by the Attorney General of our state, but I don't think that is the point that we are discussing here today. I do not doubt that

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there will be litigation with respect to this very issue, and I submit to you that there may be some very difficult questions of law that will be presented to the courts as it relates to bonds that were issued prior to 1973 because, as everyone here knows, because of legislation passed last year in connection with the county ruling, any further bonds issued by the Port Authority will not contain the covenant, but I think the real point here is that there was a change in attitude, not just in the Legislature of both states between 1962 and 1974 but there has been a very real change in the dimension of the problems of moving people and goods both in New York and New Jersey, and that we are dealing here with a question not only of good faith. We are also dealing with the question of priorities and what may have been legislative priorities in 1962 simply are not those priorities in 1974, and it is my hope and my belief at this time, although certainly I do not profess to be an expert in both federal and state constitutional law, but a case can be made for what we are doing here today, and I would rather assume that risk than to do nothing."

"MR. KOPPELL: Thank you, George. Mr. Speaker."

"ACTING SPEAKER FIELD: Mr. Koppell."

"MR. KOPPELL: I think that Assemblyman Farrell's words are extremely accurate and appropriate to what we are doing here today. As one who has been a leader of this fight now for four years, I regard this as a most significant moment for the development of mass tranportation in the metro-

politan area. Not only does this promise to open up the financial resources of the Port Authority, which many have estimated over or up to $100 million a year in surplus revenues to mass transportation, but it will allow the Port Authority to assume the role which was given to it back in the early 1920's when it was created, and that was as the essential coordinating force for mass transportation through the metropolitan area. That role was written into the original compact passed by the two states and ratified by the Congress of the United States, and I and many others have felt that the 1962 Legislature which we are repealing today went counter to that original compact and was in a sense contrary to the interpretation of its purposes and never really had any role, never really had any place in the statute books of this state and the state of New Jersey. In fact, I as a plaintiff in a lawsuit have argued that the 1962 legislation could never be deemed effective because it was never ratified by Congress and it represented such a radical departure from the intent of Congress in ratifying the original compact between the states, that in order for it to be effective Congress had to act on it and Congress never did. Thank goodness now Congress will never have to act upon it because we are repealing this covenant today should this bill pass, and I want to urge upon Governor Wilson that he sign it expeditiously and that the matter be given to the courts and I am confident that the court will recognize that this Legislature must have the right to provide the kind of funds that are necessary to have an efficient and reasonable in

costs mass transportation system in the region. If anything indicates the necessity of increased funds for mass transporation, it is the energy crisis in which we are involved and which threatens our whole society. I think this legislation is critical. I think this legislation is certainly one of the most important things that we can do today, and is undoubtedly one of the most important steps that we can take to improve mass transportation. I want to commend the sponsors and the leadership of the House for bringing it forth so that finally we can make the Port Authority what it ought to be and we devote the mass resources that that Authority has to solving one of the critical problems we have in our state, that of mass transportation. I urge a unanimous house vote in support of this legislation."

"Mr. Meyer: Mr. Speaker."

"Acting Speaker Field: Mr. Meyer."

"Mr. Meyer: Mr. Speaker, I recall in the winter of 1971 when I came up here as a rookie Assemblyman sitting in the corporations, authorities and commissions committee of this House and seeing another rookie Assemblyman across the table from me from Riverdale, from the Bronx, start to talk about the Port Authority of New York, an agency which I never heard of. Maybe I read about it in the papers a few times. And he kept talking about the idealism of it, kept talking about the need of public transportation in this state. Then I remember him shortly thereafter forge an ad hoc committee because he couldn't get any formal recognition of what he was

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doing from the majority party at that time, holding hearings in New York, holding many meetings, giving some due, needed publicity to this fact, and I just want to say after what I say in 1971, 1972, 1973 and 1974 from Ollie Koppell that I take my hat off to him for what he did."

"MR. STRELZIN: Mr. Speaker."

"ACTING SPEAKER FIELD: Mr. Strelzin."

"MR. STRELZIN: Will Mr. Farrell yield?"

"ACTING SPEAKER FIELD: The member yields."

"MR. STRELZIN: Mr. Farrell, I am under the impression that the New York Port Authority Charter provided that if there was a shortage of funds to make necessary payments to bond holders that money would be supplied by the State of New York on application to the governmental Comptroller. Am I right, sir?"

"MR. FARRELL: Both states."

"ACTING SPEAKER FIELD: Read the last section."

"THE CLERK: This act shall take effect immediately."

"ACTING SPEAKER FIELD: Call the roll. (Roll call.) The bill is passed. (Applause.)"

"MR. STRELZIN: Mr. Speaker."

"ACTING SPEAKER FIELD: Mr. Strelzin."

"MR. STRELZIN: Mr. Speaker, if I might, I was busily engaged in a little discussion but I want to

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pay my compliments to Assemblyman Farrell and Assemblyman Koppell on this legislation we just passed. It has been a long road and I hope that when it goes downstairs the Governor will join with us, but I think it is a step that I know will go a long way towards solving our problems in the metropolitan area, and I hope this problem doesn't spread to the rest of the state."

The statement of sponsors appended to the bill in New Jersey (A1304) provided:

"STATEMENT

This bill is designed to preclude the application of the 1962 covenant restricting port authority participation in mass transit projects. Chapter 208, P.L. 1972, precluded such application to bonds newly issued after the effective date of that act, but maintained in status quo the position of holders of bonds issued between March 27, 1962 and December 28, 1972. Since affected bonds are outstanding until the year 2007, the restrictions imposed by the covenant effectively preclude sufficient port authority participation in the development of a public transportation system in the port district. In 1972 the State of New York passed legislation precluding the application of the 1962 covenant from outstanding bonds as well as newly issued bonds. It is the purpose of this act to accomplish effective repeal of the covenant."

13. United States Trust Company of New York among others tried to persuade Governor Wilson not to sign the

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legislation. Governor Wilson issued the following statement when he signed into law the 1974 New York legislation repealing Section 3 of the 1962 Covenant.

> "Coupled with action taken by the State of New Jersey, this bill retroactively repeals the 1962 statutory covenant entered into between the States of New York and New Jersey and prospective purchasers of bonds of the Port Authority of New York and New Jersey. Pursuant to that covenant, the Port Authority is prohibited from using its revenues beyond the existing Port Authority Trans-Hudson (PATH) System for rail mass transit facilities unless such facilities would be self-supporting.
>
> "It is with great reluctance that I approve a bill that overturns a solemn pledge of the State. I take this extraordinary step only because it will lead to an end of the existing controversy over the validity of the statutory covenant, a controversy that can only have an adverse affect upon the administration and financing of the Port Authority, and because it will lead to a speedy resolution by the courts of the questions and issues concerning the validity of the statutory covenant. Because it is the province of the courts to decide questions of constitutionality, I will not prevent the covenant issue from being brought before them, especially where it is the unanimously expressed desire of the members of both houses of the New York State Legislature as well as the expressed will of the Governor and both houses of the Legislature of the State of New Jersey to do so.

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> "In approving the bill, I note that the Chairman of the Port Authority has advised me that the Authority presently has invested more than $220 million in PATH facilities and has incurred operating deficits for PATH services of approximately $140 million. Moreover, the Authority expects to spend nearly $130 million over the next ten years to complete the renovation of the existing PATH System and an additional $350 million for the PATH rail extensions and high speed rail service to John F. Kennedy International Airport. Thus, the Port Authority is solidly committed to providing mass transportation facilities and services to New Yorkers.
>
> "In response to my inquiry, the Chairman has also advised me that because of the heavy long term capital commitments for the PATH facilities and the Kennedy rail link, the Authority has no significant capacity to contribute funds for operating subsidies for commuter railroads. Hence, the plain and simple fact of the matter appears to be that the Authority has virtually no excess funds that could be channeled into operating subsidies for mass transportation facilities in the New York metropolitan area. Even if such funds were available, existing bond indenture provisions which survive despite repeal of the statutory covenant would prohibit their use except in relation to facilities owned, leased or operated by the Port Authority.
>
> "For these reasons, my approval of the bill should not be considered as a criticism of the efforts which the Port Authority has made to provide effective

transportation services, including mass transportation services, to the people of the New York metropolitan area, nor a panacea for the mass transportation problems plagueing the New York metropolitan area. The bill is approved."

Governor Byrne's office issued the following statement when he signed into law the New Jersey legislation repealing the 1962 Covenant:

"Governor Brendan Byrne Tuesday signed a bill designed to stimulate greater involvement in mass transit projects by the Port Authority of New York and New Jersey.

"The bill, A-1304, sponsored by Assemblyman Herbert C. Klein, D-Passaic, repeals the 1962 covenant which has effectively precluded the port authority from becoming involved in mass transit projects in the New York metropolitan area. The covenant restricts the authority from participation in mass transit projects which are not self-sustaining.

" 'I hope this bill, coupled with the same legislation in New York State, will clear the way once and for all for the port authority to fulfill what I believe was one of its original functions,' said Byrne. 'The authority was created as a transportation agency and I intend to see that it lives up to its original promise of assisting in establishment of a quality public transportation system for the metropolitan region without in any way impairing its fiscal integrity.'

" 'I hope the authority will now join with New York State, New York City and New Jersey in working toward the realization of a viable public transportation for the port district,' he added.

"The Governor said the port authority staff has the experience, expertise and financial capability to perform a valuable function in solving the mass transit dilemma in the metropolitan region.

" 'This bill means that it is the public policy of the state of New Jersey that the port authority—a creation of the states of New Jersey and New York —should become a leader in improving the plight of those who rely on or choose to use mass transit,' he said.

"The Governor said he expects repeal of the covenant to provide new impetus for the proposed PATH (Port Authority Trans-Hudson) extension to Plainfield, as well as for future transit projects in New Jersey.

"Byrne emphasized he intends to do nothing that would adversely affect the authority's financial integrity, particularly its ability to meet its obligations to its bond holders.

" 'The State has as much at stake as the authority in maintaining the sound financial base it has enjoyed,' he said. 'Preserving the authority's outstanding reputation in the financial community can only serve to enable it to become more involved in future public transportation projects.' "

14. On November 12, 1974, the New York Times published the following article:

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"Cahill Defends Port-Unit Stand

"Denies His Transit Backing Caused Fund Problems

"Princeton, Nov. 11—Former Gov. William T. Cahill today defended his efforts to effect a greater involvement of the Port Authority of New York and New Jersey in mass transportation during his term in office.

"Over the weekend, Port Authority officials accused him of having precipitated the agency's current financial problems by attempting to force it into deficit commuter rail operations.

"'When something goes wrong' Mr. Cahill said, 'everybody wants to blame everybody else. When I went in there, nothing was happening. My administration got them involved in mass transportation.'

"Mr. Cahill, who now practices law here, was Governor from January, 1970, until January of this year. He was elected after repeated campaign promises to push the Port Authority into mass transportation.

"The Port Authority's present problems, which stem from a drop in income at various facilities and difficulty in raising money, have nothing to do with administration, Mr. Cahill insisted.

"Lists Roots of Problems

"'Their problems', he said, 'come from four sources—a reduction in revenues because of inflation,

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slackness in the bond market, the action of the two states in repealing the covenant with the bondholders retroactively and the lawsuit stemming from that repeal.'

"The covenant signed in 1962 when the Port Authority took over the commuter line now known as PATH, guaranteed purchasers of the authority's bonds that it would never have to take on another deficit passenger rail service. Both New York and New Jersey repealed the covenant earlier this year and a bondholders' suit was filed soon thereafter.

"Mr. Cahill said he would have vetoed any retroactive repeal during his administration.

"'It's like telling your bondholders that your bonds don't really mean what they say they mean,' he said. 'It's like raising a red flag in the financial community.'

"Mr. Cahill said he never asked the Port Authority to take on any projects that could not have been accomplished under the restrictions of the 1962 covenants.

"The former Governor said he was suspicious of the Port Authority's assertions that it cannot sell bonds.

"'The Sport Authority sold its bonds at 7 per cent with nothing to back them up,' he said. 'Certainly the Port Authority can do as well as that'. The New Jersey Sports and Exposition Authority is constructing a race track and stadium in the Hackensack Meadows.

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"Meadows Rail Link Sought

"Mr. Cahill conceded that there was little physical evidence that the Port Authority was acting on mass-transportation projects he had said they would undertake; an extension of PATH to Plainfield via Newark International Airport, new rail connections in the meadows and the rehabilitation of Penn Station in Newark.

" 'You've got to realize how long these things take,' he said, noting that the PATH extension had been in the planning stages for almost four years."

15. A number of bills were introduced during 1974 in the New Jersey Legislature with respect to the examination and development of various solutions to New Jersey's transportation needs. With one exception (Assembly Joint Resolution 21) none of the bills if adopted in the form introduced would have involved the use of Port Authority funds. None of the bills was reported out of committee. (Stip. 338-361)

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The foregoing stipulation is hereby agreed to and approved.

Dated: December 20, 1974

MEYNER, LANDIS & VERDON
Gateway I
Newark, New Jersey
/s/ ROBERT B. MEYNER

CARTER, LEDYARD & MILBURN
2 Wall Street
New York, New York 10005
/s/ DEVEREUX MILBURN

WILLIAM F. HYLAND
Attorney General of the State
of New Jersey
Attorney for Defendants

By /s/ MICHAEL I. SOVERN
Michael I. Sovern

/s/ MURRAY J. LAULICHT
Murray J. Laulicht

/s/ HAROLD S. H. EDGAR
Harold Edgar

(Stip. 366)

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APPENDIX V

CONSOLIDATED BOND RESOLUTION
(Adopted October 9, 1952)

WHEREAS, by Chapter 48 of the Laws of New York of 1931, as amended, and Chapter 5 of the Laws of New New Jersey of 1931, as amended, The Port of New York Authority (hereinafter called the Authority) has been authorized and empowered to establish and maintain a certain General Reserve Fund, and to pledge said fund as security for certain of its bonds or other securities or obligations, and

WHEREAS, there are now outstanding several issues of bonds of the Authority, which although secured by said General Reserve Fund, nevertheless differ as to form, security, terms and conditions, and

WHEREAS, the Authority has determined to authorize and establish an issue of Consolidated Bonds, and to use such Bonds (and the proceeds derived from the sale thereof) from time to time for the purpose of refunding bonds heretofore or hereafter issued and to serve as a unified medium for financing for any and all purposes for which the Authority is or shall be authorized to issue bonds secured by a pledge of the General Reserve Fund, to the exclusion of bonds of prior issues.

NOW, THEREFORE, after due consideration had, be it resolved by The Port of New York Authority: (p. 55) • • •

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SECTION 2. Establishment and Issuance.

An issue of bonds of the Authority to be known as "Consolidated Bonds" is hereby authorized and established. The bonds of said issue shall be direct and general obligations of the Authority and the full faith and credit of the Authority are hereby pledged for the prompt payment of the debt service thereon and for the fulfillment of all other undertakings of the Authority assumed by it to or for the benefit of the holders thereof. This resolution shall constitute a contract with the holders of such bonds.

Said Consolidated Bonds shall be issued only for purposes for which at the time of issuance the Authority is authorized by law to issue bonds secured by a pledge of the General Reserve Fund and only in such amounts as are permitted by Section 3 of this resolution. Said Consolidated Bonds shall be secured by revenues of the facilities of the Authority in the manner and to the extent provided in Sections 4 and 5 of this resolution and by the General Reserve Fund of the Authority in the manner and to the extent provided in Section 6 of this resolution and by the Consolidated Bond Reserve Fund in the manner and to the extent provided in Section 7 of this resolution.

Said Consolidated Bonds may be issued from time to time in such series as the Authority may hereafter determine. The bonds of each series may be issued in one or more installments as the Authority may hereafter determine.

All Consolidated Bonds constituting a particular series shall be uniform in respect of (a) dates of payment of interest, (b) place or places of payment of principal and interest, (c) medium of payment, (d) whether issuable as coupon bonds, or as registered bonds without coupons, or both, (e) provisions, if any, in respect of their exchange-

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ability for bonds of different denominations, and of the interchangeability of coupon bonds and registered bonds without coupons, and (f) provisions, if any, for redemption and the terms and conditions thereof, *provided, however,* that bonds constituting a particular series may be made redeemable either in the direct or the inverse order of their maturities if such bonds have differing dates of maturity or by lot. All bonds constituting the whole or a part of a particular series and maturing on the same date shall be uniform in respect of interest rate or rates. All bonds of a series consisting only of bonds having the same date of maturity shall be uniform in respect of provisions, if any, in respect of amortization and retirement of bonds of such series.

Any resolution establishing a series or authorizing the issue of an installment of bonds of a series may contain terms and provisions not inconsistent with this resolution.

SECTION 3. Limitations on Amount.

The Authority shall not issue new Consolidated Bonds at any time unless one or another of the following four conditions shall exist, either • • • or, in the alternate,

> (Condition 3) Unless at the time of issuance of such new Consolidated Bonds the sum of the net revenues specified in the following subdivisions i, ii, iii and iv (computed as hereinafter set forth in this Section 3) in the case of all facilities the surplus revenues of which shall be payable into the General Reserve Fund after the fulfillment of the purposes for which the new Consolidated Bonds are to be issued, to wit:

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> i. In the case of facilities which have been in operation during the entire period of thirty-six months next preceding such time of issuance,—the combined net revenues derived from all such facilities during any period of twelve consecutive months selected by the Authority out of the thirty-six months next preceding such time of issuance, plus
>
> ii. In the case of facilities which have been in operation during the entire period of twelve months but not during the entire period of thirty-six months next preceding such time of issuance,—the net revenues derived from each such facility during any period of twelve consecutive months (which need not necessarily be the same for each such facility) selected by the Authority out of such period of operation, plus
>
> iii. In the case of facilities which have not been in operation during the entire period of twelve months next preceding such time of issuance (including facilities under construction at such time or which are to be acquired, established or constructed with the proceeds of the sale of the new Consolidated Bonds),—the average annual net revenues which the Authority estimates will be derived from each of such facilities during the first thirty-six months after such time of issuance, but if in the opinion of the Authority any such facility will not be placed in operation until after such time of issuance, then as to each such facility, the average annual net revenues which the Authority estimates will be derived during the first thirty-

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six months of operation thereof after such time of issuance; *provided, however,* that no revenues estimated under this subdivision iii shall be included in the sum of all net revenues computed under this Condition 3 unless at the time of issuance of the new Consolidated Bonds there shall be in or available for payment into the General Reserve Fund an amount equal to the full amount prescribed in the General Reserve Fund statutes, calculated without the new Consolidated Bonds; and *provided,* further, that the amounts of any revenues estimated under this subdivision iii plus the amounts of any revenues estimated under the next following subdivision iv shall in no event exceed twenty-five per centum of the sum of all net revenues computed under the preceding subdivisions i and ii of this Condition 3, plus

iv. In the case of each capital improvement to any of such facilities if such capital improvement is either under construction at such time of issuance or has been completed less than twelve months prior to such time or, in case it has not yet been commenced, if the Authority has either issued bonds or has entered into a contract for the issuance of bonds or has authorized the issuance of the new Consolidated Bonds for the financing of all or part of such capital improvement,—the average annual amount which the Authority estimates that the net revenues of the facility to which such improvement appertains will be increased during the first thirty-six months after the completion of such improvement, over and above the amount of

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net revenues included for such facility in the foregoing subdivisions i, ii or iii of this Condition 3; *provided, however,* that no revenues estimated under this subdivision iv shall be included in the sum of all net revenues computed under this Condition 3 unless at the time of issuance of the new Consolidated Bonds there shall be in or available for payment into the General Reserve Fund an amount equal to the full amount prescribed in the General Reserve Fund statutes, calculated without the new Consolidated Bonds; and *provided,* further, that the amount of any revenues, estimated under this subdivision iv plus the amounts of any revenues estimated under the next preceding subdivision iii shall in no event exceed twenty-five per centum of the sum of all net revenues computed under the preceding subdivisions i and ii of this Condition 3,

shall have amounted to at least one and three-tenths times the prospective debt service (computed on the assumptions hereinafter set forth in this Section 3) for the calendar year after such time of issuance for which the combined debt service (so computed) upon the following bonds would be at a maximum, to wit:

i. The new Consolidated Bonds,

ii. All bonds outstanding at such time of issuance which are secured by a pledge of the General Reserve Fund, not including, however, any bonds which the resolution authorizing the issuance of the new Consolidated Bonds shall specifically

designate are to be refunded by the new Consolidated Bonds, and

iii. Additional bonds secured by a pledge of the General Reserve Fund and having annual debt service in amounts estimated by the Authority, if estimated revenues and/or estimated revenue increases in connection with any facility or capital improvement have been included under the next preceding subdivisions iii and/or iv in the computation of the sum of the net revenues under this Condition 3 in connection with the particular new Consolidated Bonds to be issued and if the Authority is of the opinion at the time of issuance of such new Consolidated Bonds that such additional bonds will be issued in connection with such facility or improvement and will be outstanding during the thirty-six months for which the revenues and/or revenue increases have been estimated under said subdivison iii and/or iv;

or, in the alternate, (pp. 57, 59-60)•••

Prospective debt service upon any bonds shall be computed for the purpose of determining the calendar year for which such debt service will be at a maximum and the amount of such debt service for such year, within the meaning of this Section 3, upon the assumptions that the principal amount of such bonds will not be paid prior to maturity except in fulfillment of contractual obligations by the Authority to the holders thereof for the redemption thereof prior to maturity, and that in those cases such redemption will be effected at the latest date permitted by such agreement.

SECTION 4. Pledge of Revenues.

The payment of the debt service upon all Consolidated Bonds, regardless of the series or installment of which they form a part, and regardless of the dates of their issuance or maturity or the purposes for which issued, shall be secured equally and ratably by the net revenues of the Authority from each of the following:

i. The Holland Tunnel, the Lincoln Tunnel, the George Washington Bridge, the Bayonne Bridge, the Goethals Bridge, the Outerbridge Crossing, Port Authority Inland Terminal No. 1 (also known as the Port Authority Building), the New York Union Motor Truck Terminal, the Newark Union Motor Truck Terminal, the Port Authority Bus Terminal, La Guardia Airport, New York International Airport, Newark Airport, Teterboro Airport, the Port Authority Grain Terminal, Port Newark and the Hoboken-Port Authority Piers, and

ii. Any additional facilities, the establishment, acquisition, effectuation, construction, rehabilitation or improvement of which is financed or refinanced in whole or in part by the issuance of Consolidated Bonds;

and, except as otherwise provided herein the net revenues of each of said facilities are hereby irrevocably pledged to the payment of the debt service upon all Consolidated Bonds as the same may fall due, and shall be applied as provided in Section 5 hereof, and all Consolidated Bonds shall constitute a lien and charge thereon.

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The foregoing pledge and lien are, however, subject to and shall be subordinate to (but only to) the following prior pledges and liens:

(a) In the case of the revenues of the Holland Tunnel, the Lincoln Tunnel, the George Washington Bridge, the Bayonne Bridge, the Goethals Bridge, the Outerbridge Crossing, Port Authority Inland Terminal No. 1 (the Port Authority Building), the New York Union Motor Truck Terminal, the Newark Union Motor Truck Terminal, the Port Authority Bus Terminal and the Port Authority Grain Terminal,—to pledges heretofore made and liens heretofore created in favor of the aforesaid General and Refunding Bonds;

(b) In the case of the revenues of La Guardia Airport, New York International Airport, Newark Airport and Teterboro Airport,—to pledges heretofore made and liens heretofore created in favor of the aforesaid Air Terminal Bonds;

(c) In the case of the revenues of Port Newark, —to pledges heretofore made and liens heretofore created in favor of the aforesaid Marine Terminal Bonds.

Consolidated Bonds shall not be issued for any purpose in connection with any facility unless after the accomplishment of such purpose the debt service upon all Consolidated Bonds shall constitute a first lien and charge upon the net revenues of the Authority from such facility subject, however, to (but only to) the prior liens recited in the preceding paragraph.

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SECTION 5. Application of Revenues.

Subject to the prior pledges and liens described in Section 4 of this resolution, all net revenues pledged as security for Consolidated Bonds shall be applied to the following purposes in the following order:

(a) To the payment of debt service upon all Consolidated Bonds;

(b) All remaining balances of net revenues pledged as security for Consolidated Bonds shall be paid into the Consolidated Bond Reserve Fund established by Section 7 of this resolution, except such amounts as may be necessary to maintain the General Reserve Fund in the amount prescribed by the General Reserve Fund statutes.

The pledge of net revenues made in Section 4 of this resolution (and the lien and charge of Consolidated Bonds upon such net revenues) shall be subject to the right of the Authority to make payments into the General Reserve Fund to the extent above provided in this Section 5, and to that extent only.

SECTION 6. General Reserve Fund.

The payment of the debt service upon all Consolidated Bonds, regardless of the series or installment of which they form a part, and regardless of the dates of their issuance or maturity or the purposes for which issued, shall be further secured equally and ratably by the General Reserve Fund; and the pledge thereof and of the money which may be or become part thereof, contained in the resolution of the Authority, adopted March 9, 1931, establishing said

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General Reserve Fund, as amended May 5, 1932, is hereby expressly extended to and made applicable to (and for such purpose the General Reserve Fund is hereby irrevocably pledged as security for) all Consolidated Bonds for the benefit of the holders thereof, in the manner and to the extent set forth in the aforesaid resolution of March 9, 1931, as amended May 5, 1932, *pari passu* with bonds heretofore issued by the Authority and with the holders of such bonds; *provided,* that nothing herein shall be construed to grant or confer greater rights in or to said General Reserve Fund upon the holders of Consolidated Bonds than are now granted or conferred upon the holders of the bonds of prior issues.

The foregoing pledge is subject to (but only to) the following separate rights which the Authority hereby reserves to itself:

(a) The right to pledge said General Reserve Fund as security for any bonds whatsoever hereafter issued by the Authority as security for which it may at the time be authorized by law to pledge the General Reserve Fund; and

(b) The right to use the moneys in said General Reserve Fund to meet, pay or otherwise fulfill any of the undertakings which it has assumed, does now assume by this resolution or shall hereafter assume to or for the benefit of the holders of any bonds as security for which said General Reserve Fund has heretofore been or is now pledged, or for which said General Reserve Fund may hereafter be pledged as above provided;

provided, that no greater rights in or to the General Reserve Fund shall hereafter be granted to or conferred

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upon the holders of any bonds now outstanding or any bonds hereafter issued than are granted to and conferred upon the holders of all Consolidated Bonds.

Except as provided in the next sentence of this paragraph, the moneys in the General Reserve Fund shall not be used for any purpose at any time if there are any other moneys of the Authority available for that purpose at such time, and shall not be used for the payment of debt service prior to the time when the interest, sinking fund payments, redemption prices, principal amounts and other items constituting such debt service shall be required to be paid or set aside by the Authority; and the moneys in said General Reserve Fund shall be deposited in such depositories as the Authority may designate or invested in obligations of or guaranteed by the United States. If, however, there shall at any time be in or available for payment into all debt reserve funds of the Authority an aggregate amount of moneys in excess of an amount equal to two years' debt service upon all those bonds of the Authority which are secured by a pledge of the General Reserve Fund and which are outstanding at that time, to the extent that such moneys in or available for payment into such debt reserve funds will be available to pay debt service upon such bonds during the ensuing twenty-four calendar months, then and in any such event such excess moneys may be used at such time for any purpose for which said moneys may be used under the General Reserve Fund statutes, whether or not there are other moneys available for that purpose; and such excess moneys may be deposited in such depositories as the Authority may designate or invested in bonds, notes or other obligations of or guaranteed by the United States, the State of New York or the State of New Jersey, and any

bonds of the Authority theretofore actually issued and negotiated and secured by a pledge of the General Reserve Fund. Two years' debt service, when used in this paragraph with respect to bonds outstanding at any time, shall mean the amounts which the Authority is obligated by contract with the holders of such bonds to pay as debt service upon such bonds during the ensuing twenty-four calendar months; *provided, however,* that in computing such two years' debt service on any such outstanding bonds which are short-term bonds there shall be substituted for the actual debt service on such short-term bonds during said ensuing twenty-four calendar months the debt service which would be payable during said twenty-four calendar months if such short-term bonds were forthwith refunded by bonds having the following characteristics: maturity—thirty years from such time; interest—at the same rate as upon the short-term bonds and payable semi-annually beginning six months from such time; amortization—in such annual amounts as would be required to retire the principal amount of the short-term bonds outstanding at such time by the thirtieth anniversary of such time if such annual retirement were effected at par at each anniversary of such time and if the annual debt service thereon would be equal for all years thereafter until such thirtieth anniversary.

The resolution of the Authority, adopted March 9, 1931, establishing said General Reserve Fund, as amended May 5, 1932, is hereby further amended to conform to the provisions of this Section 6; *provided, however,* that nothing contained in this Section 6 shall be construed to limit, curtail or impair any pledge of the General Reserve Fund or regarding its administration, investment and use made in favor of or for the benefit of the holders of any bonds of

prior issues or to prevent the Authority from doing any act or thing required to be done in the fulfillment of any such pledge.

SECTION 7. Consolidated Bond Reserve Fund.

There is hereby established a special fund (herein called the Consolidated Bond Reserve Fund) the moneys in which are hereby pledged as additional security for all Consolidated Bonds, into which shall be paid all balances of net revenues pledged as security for Consolidated Bonds, remaining after deducting the amounts for which provision is made in subdivisions (a) and (b) of Section 5 of this resolution. The moneys in the Consolidated Bond Reserve Fund shall be accumulated or in the discretion of the Authority shall be applied to any of the following purposes and to such purposes only:

(a) To the payment of Consolidated Bonds at maturity, but in case a sinking fund has been established for the retirement of bonds of the series of which such bonds form a part only if the available moneys in such sinking fund are insufficient for such purpose, and in the case of other Consolidated Bonds, only if the net revenues pledged as security for Consolidated Bonds for the calendar year in which such payment shall be due and which are available for such payment are insufficient for such purpose.

(b) To the payment of debt service upon Consolidated Bonds then outstanding (other than the payment of such bonds at maturity), but only if the net revenues pledged as security for Consolidated Bonds

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for the calendar year in which such payment shall be due and which are available for such payment are insufficient for such purpose.

(c) To the purchase for retirement of Consolidated Bonds of any series as determined by the Authority at such prices as the Authority may determine to be reasonable; *provided, however,* that in case all of the bonds of such series are subject to redemption six months or less from the date on which the bonds are to be purchased for retirement, then such prices shall not exceed the highest price at which all of the bonds of such series might be redeemed at or prior to the expiration of said six months. Such purchases may be made at the discretion of the Authority, at public or private sale, with or without advertisement and with or without notice to other holders of Consolidated Bonds, and bonds theretofore issued and negotiated and then held by the Authority for investment may be purchased, as well as bonds held by others. In ascertaining whether the purchase price of any bond comes within the maximum above specified, brokerage commissions and similar items shall not be taken into consideration. The bonds so purchased shall be forthwith cancelled.

(d) To the redemption of Consolidated Bonds of any one or more series as may be determined by the Authority, if such bonds are subject to redemption. The bonds so redeemed shall be forthwith cancelled.

(e) To the payment of expenses incurred for the operation, maintenance, repair and administration

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of any facility the net revenues of which are pledged as security for Consolidated Bonds (including the expenses specified in the definition of net operating revenues in Section 1 of this resolution), but only to the extent that the gross operating revenues of such facility for the calendar year in which such payment shall be due, are insufficient or unavailable for such purpose.

(f) To the payment of debt service upon bonds other than Consolidated Bonds which are described in the last paragraph of this Section 7.

(g) To any other or additional purposes for which the Authority is now or may hereafter be authorized by law to expend the revenues of its facilities. (pp. 62-65) • • •

SECTION 12. Miscellaneous Covenants.

The Authority covenants and agrees with the holders of Consolidated Bonds, and with each such holder, as follows:

(a) Fully and faithfully to perform all duties required by the Constitutions and Statutes of the United States and of the States of New York and New Jersey, and by the Compact of April 30, 1921, between said two States, with reference to all facilities the net revenues of which are pledged as security for Consolidated Bonds,—those hereafter established, constructed or acquired by it, as well as those presently owned, leased or operated by it.

(b) Not to issue any more General and Refunding Bonds of the issue established March 18, 1935, Air

Terminal Bonds of the issue established June 18, 1948 or Marine Terminal Bonds of the issue established November 23, 1948 in addition to the bonds of those issues outstanding at the adoption of this resolution. This covenant and agreement shall not only be with and for the benefit of holders of Consolidated Bonds but shall also be with and for the benefit of holders of outstanding bonds of prior issues and shall not be subject to modification except in accordance with the provisions of the resolutions establishing such prior issues in addition to the provisions of Section 16 of this resolution.

(c) To proceed promptly and in an economical and efficient manner with the effectuation, establishment, acquisition, construction, rehabilitation or improvement of all facilities, the effectuation, establishment, acquisition, construction, rehabilitation, or improvement whereof is financed with Consolidated Bonds.

(d) To maintain in good condition all facilities the surplus revenues of which are payable into the General Reserve Fund, and to operate them in an efficient and economical manner, making all such renewals and replacements and acquiring and using all such equipment as the Authority shall determine to be necessary or desirable for the proper and economical maintenance and operation thereof.

(e) To make such improvements as part of or in connection with facilities the surplus revenues of which are payable into the General Reserve Fund as the Authority shall determine to be necessary or

desirable as incidental to or in connection with the operation of said facilities.

(f) To establish and collect flight fees, wharfage, dockage, rents, tolls and other charges in connection with facilities the net revenues of which are pledged as security for Consolidated Bonds, to the end that at least sufficient net revenues may be produced therefrom at all times to provide for the debt service upon all Consolidated Bonds.

(g) In the event the net revenues pledged as security for Consolidated Bonds are insufficient to provide for the debt service upon any or all Consolidated Bonds, to make good any deficiency out of the General Reserve Fund or other available revenues, moneys or funds; and for that purpose to establish, maintain and collect flight fees, wharfage, dockage, rents, tolls and other charges in connection with facilities the surplus revenues of which are payable into the General Reserve Fund (including facilities the net revenues of which are not pledged as security for Consolidated Bonds), to the end that combined surplus revenues may be produced therefrom at least sufficient to make good (through the medium of the General Reserve Fund) any deficiency in the debt service upon Consolidated Bonds, *provided, however,* that nothing herein contained shall be deemed to constitute an agreement or covenant by the Authority to make any payments into the General Reserve Fund in excess of the payments required to be made pursuant to the General Reserve Fund statutes.

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(h) To keep all facilities the surplus revenues of which are payable into the General Reserve Fund (and all structures, equipment and properties forming part thereof) insured, if such insurance is obtainable at reasonable rates and upon reasonable conditions, against such risks, in such amounts and with such deductibles as the Authority shall deem necessary for the protection of the holders of Consolidated Bonds.

(i) Duly and punctually to pay or cause to be paid the debt service upon all underlying mortgage bonds outstanding in connection with all or any part of any facility the surplus revenues of which are payable into the General Reserve Fund, in strict conformity with the terms of such bonds.

(j) To make all such expenditures as the Authority shall determine are necessary or desirable for, in connection with or incidental to the fulfillment of any of the covenants or other undertakings assumed by the Authority to or for the benefit of the holders of any Consolidated Bonds in this Section 12 or in any other section of this resolution or in any other resolution relating to Consolidated Bonds.

(k) In case any facility or any real property constituting a portion of a facility, the net revenues of which are pledged as security for Consolidated Bonds, is sold by the Authority or is condemned pursuant to the power of eminent domain, to apply the net proceeds of such sale or condemnation to capital expenditures upon facilities the net revenues of which are pledged as security for Consolidated

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Bonds, or to the retirement of Consolidated Bonds or bonds of prior issues after satisfying any prior obligations in respect of such facilities or in respect of the disposition of such proceeds; *provided, however,* that nothing herein contained shall be construed to prevent the Authority from applying the award in any condemnation proceeding in accordance with the Agreement with respect to the Newark Marine and Air Terminal between the City of Newark and the Authority, dated October 22, 1947, or the Agreement with respect to Municipal Air Terminals between the City of New York and the Authority, dated April 17, 1947, or any lease or other agreement for the use of real property heretofore or hereafter entered into by the Authority whether as landlord, tenant, licensor, licensee or otherwise. (pp. 67-68)

• • •

SECTION 16. Modifications.

(a) The Authority may from time to time and at any time, without authorization, consent or other action by any of the holders of Consolidated Bonds, modify or amend this resolution, or any other resolution relating to Consolidated Bonds, but only for the purpose of curing any ambiguity or of curing or correcting any defective or inconsistent provision, or for any other purpose not inconsistent with this resolution or with any other resolution relating to Consolidated Bonds; *provided,* that no such amendment made pursuant to this sub-section (a) shall alter or impair the obligation of the Authority, which is absolute and unconditional, to pay the principal and interest of any bond at the time and place and at the rate

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or amount and in the medium of payment prescribed therein, or shall alter or impair the security of any bond, or otherwise alter or impair any rights of any bondholder.

(b) In addition to the power given in sub-section (a) of this Section 16, any of the terms or provisions of this resolution (or of any resolution amendatory of or supplemental to this resolution) may be amended, repealed or modified in the manner hereinafter set forth in this Section 16, for the purpose of modifying or amending in any particular any of the terms or provisions (including, without the generality of the foregoing, any provisions regarding amortization and retirement) of any of the Consolidated Bonds or of any of the coupons pertaining thereto; *provided,* that no such amendment, repeal or modification shall alter or impair the obligation of the Authority, which is absolute and unconditional, to pay the principal and interest of any Consolidated Bond at the time and place and at the rate or amount and in the medium of payment prescribed therein, without the express consent of the holder of such bond.

i. Whenever the Authority shall desire any such amendment, repeal or modification of any of the provisions of this resolution (or of any resolution amendatory of or supplemental to this resolution), it shall call a meeting of the holders of Consolidated Bonds (or if the amendment, repeal or modification proposed shall affect the rights of the holders of such bonds of only one or more particular series or installments, then of the holders of all Consolidated Bonds of each such series or installment so to be affected) for the purpose of considering and acting upon any such proposed amendment, repeal or modi-

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fication. A notice specifying the purpose, place, date and hour of such meeting shall be published by the Authority in a daily newspaper of general circulation in the City of New York, State of New York, and also in one or more daily newspapers of general circulation in one or more of the following cities: the City of Boston, Commonwealth of Massachusetts; the City of Philadelphia, Commonwealth of Pennsylvania; the City of Chicago, State of Illinois; and the City of San Francisco, State of California. Such notice shall be published once a week for four consecutive weeks, the first publication to be not less than thirty days nor more than ninety days prior to the date fixed for the meeting. Such notice shall briefly set forth the nature of the proposed amendment, repeal or modification, and shall give notice that a copy thereof is on file with the Authority for inspection by the holders of the bonds. On or before the date of the first publication of the notice, a similar written or printed notice shall be mailed by the Authority, postage prepaid, to the holders of such bonds registered either as to principal or as to both principal and interest, at the addresses appearing on the registry books of the Authority, and who are to be affected by the proposed amendment, repeal or modification. The actual receipt by any bondholder of notice of such meeting shall not be essential to the validity of such meeting and a certificate by the Authority, duly executed by its Chairman or Vice-Chairman, that the meeting has been called and notice thereof given as herein provided, shall be conclusive as against all parties, and it shall not be open

to any bondholder to show that he failed to receive notice of such meeting or to object to the form of such notice, *provided,* that such notice shall conform substantially to the provisions of this subdivision i of this sub-section (b) of this Section 16.

ii. No person shall be entitled to vote at such meeting unless he shall be a holder of a Consolidated Bond or shall hold a proxy duly executed by such a bondholder, and (1) he shall present at the meeting his Consolidated Bond or Bonds (or in the case of the holder of a proxy, the Consolidated Bond or Bonds of his principal), or (2) he shall present at the meeting a certificate of the character herein described in subdivision iii of this sub-section (b) of this Section 16, or (3) his name (or, in the case of the holder of a proxy, the name of his principal) shall appear as a registered bondholder on the list prepared and presented to the meeting by the Registrar as provided in subdivision iii of this sub-section (b) of this Section 16.

iii. Any holder of Consolidated Bonds may, prior to any such meeting, deliver his Consolidated Bond or Bonds, at his own expense, to any Registrar of Consolidated Bonds, or to such bank, banking firm or trust company as shall be satisfactory to the Authority, and thereupon shall be entitled to receive an appropriate receipt for the bonds so deposited, calling for the re-delivery of such bonds at any time after the meeting. A certificate signed by any such Registrar, or by any such bank, banking firm or trust company that the bonds have been so deposited, and

giving the amount, denomination, series and numbers thereof, shall be sufficient evidence to permit the holder of any such certificate, including the holder of a proxy who shall produce such certificate, to be present and to vote at any meeting. The Registrar or Registrars of Consolidated Bonds shall prepare and deliver to the Authority at the time of the convening of the meeting a list of the names and addresses of the registered holders of the bonds proposed to be affected by said amendment, repeal or modification, as of the close of business on the day before the date set for the meeting, or the date to which such meeting shall have been adjourned, together with a statement of the denominations, series and numbers of the bonds registered in the name of each such registered holder.

iv. The Authority shall present to the meeting at the convening thereof a statement in writing duly executed by its Chairman or Vice-Chairman or by the Chairman or Vice-Chairman of its Committee on Finance, listing the denominations, series and numbers of all bonds of all series proposed to be affected by said amendment, repeal or modification, owned by it or held for its account directly or indirectly, including any bond registered in the name of the Authority or held for the account of any debt reserve fund of the Authority, and no person shall be permitted at the meeting to cast any vote or give any consent because of any bonds listed on such statement, and no such bonds (hereinafter referred to as Authority-owned bonds) shall be counted in determining any vote at such meeting, including the determination of whether or not a quorum is present.

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v. A representation of at least 60% in aggregate principal amount of the Consolidated Bonds then outstanding (exclusive of Authority-owned bonds) or, if the amendment, repeal or modification proposed shall only affect the rights of the holders of one or more particular series or installments of Consolidated Bonds, then 60% in aggregate principal amount of the bonds outstanding (exclusive of Authority-owned bonds) of each such series or installment so to be affected, shall be necessary to constitute a quorum at any such meeting of bondholders; but less than a quorum may adjourn the meeting from time to time and the meeting may be held as adjourned without further notice, whether such adjournment shall have been held by a quorum or by less than a quorum. The Authority shall designate a Commissioner or officer of the Authority to preside as temporary chairman, and such temporary chairman shall immediately call for nominations for a permanent chairman for such meeting. Such permanent chairman shall be some person who shall be a bondholder, or the holder of a proxy, entitled to vote at the meeting. At such meeting each person shall be entitled to one vote for each $1,000 principal amount of such bonds held or represented by him as provided in subdivision ii of this sub-section (b) of this Section 16, and such vote shall be cast by ballot. Except as herein provided, the meeting may adopt its own rules of procedure.

vi. At any such meeting as aforesaid, the Authority shall submit for consideration and action of the holders of Consolidated Bonds or, if the amend-

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ment, repeal or modification proposed shall only affect the rights of the holders of one or more particular series or installments of Consolidated Bonds, then of the bondholders of each such series or installments to be affected, a proposed resolution embodying the amendment, repeal or modification to be considered by the meeting. If such proposed resolution shall be consented to and approved (either in person or by proxy) by the holders of at least 60% in aggregate principal amount of the bonds to be affected thereby outstanding at the time (exclusive of Authority-owned bonds), then, and in such case, the Authority shall thereby be authorized and empowered to adopt such resolution, and any such resolution so adopted by the Authority shall be binding upon all bondholders, whether or not present at such meeting in person or by proxy, *provided* that no such amendment, repeal or modification shall affect the rights of the holders of one or more series or installments of Consolidated Bonds in a manner or to an extent differing from that in or to which the rights of holders of any other series or installments of Consolidated Bonds are affected unless such resolution shall be approved (either in person or by proxy) by the holders of at least 60% in aggregate principal amount of the Consolidated Bonds then outstanding (exclusive of Authority-owned bonds) of each such series or installment so affected; and no bondholder shall have any right or cause to object to the adoption of any such resolution by the Authority or to object to any of the terms or provisions therein contained or the exercise thereof or of the authorizations con-

tained therein, or in any manner to question the propriety of the adoption thereof or to enjoin or restrain the Authority from executing the same or from taking any action pursuant to the provisions thereof.

vii. Upon the adoption by the Authority of any resolution pursuant to the provisions of this Section 16, this resolution (and any resolution supplemental to or amendatory of this resolution) shall be and be deemed to be modified and amended in accordance therewith, and the respective rights, duties and obligations of the Authority and all holders of outstanding bonds shall be thereafter determined, exercised and enforced subject, in all respects, to such modifications and amendments.

viii. Minutes of all resolutions adopted and proceedings had at every such meeting shall be made and duly entered in books to be from time to time provided for that purpose by the Authority, and any such minutes as aforesaid, if signed by the chairman of the meeting at which such resolutions were passed or proceedings had, shall be prima facie evidence of the matters therein stated, and until the contrary is proved, every such meeting in respect of the proceedings of which minutes shall have been so made and signed shall be deemed to have been duly held and conveyed, and all resolutions passed thereat or proceedings had thereat shall be deemed to have been duly passed and had.

As use above in this Section 16, the terms "bond" and "Consolidated Bond" shall include any interim receipt

therefor; and the terms "bondholder" and "holder" of a "Consolidated Bond" shall include the holder of such an interim receipt.

SECTION 17. Determinations.

Whenever in this resolution it is provided that any selection, designation, determination or estimate shall or may be made by the Authority or that any action may be taken or withheld by the Authority or that any action shall or may be taken or withheld at the option of or dependent upon the opinion, discretion or judgment of the Authority, then the Authority's such selection, designation, determination, estimate, action, option, opinion, discretion or judgment expressed by its Board of Commissioners or by a committee or officer or other person duly authorized shall be conclusive for the purposes of this resolution.

APPENDIX VI

RESOLUTION ESTABLISHING FORTY-FIRST SERIES OF CONSOLIDATED BONDS, DUE 2008
(September 13, 1973)

WHEREAS, heretofore and on the 9th day of October, 1952, The Port Authority of New York and New Jersey (formerly known as The Port of New York Authority and hereinafter called the Authority) adopted a resolution providing for the issuance of certain direct and general obligations of the Authority, hereinafter called Consolidated Bonds, from time to time, in conformity with said resolution for the purposes therein set forth, which resolution is hereinafter called the Consolidated Bond Resolution,

and which resolution constitutes a contract with the holders of the bonds so issued; and

WHEREAS, said Consolidated Bond Resolution provides that such Consolidated Bonds shall be issued in such series as the Authority may determine, and that the characteristics of the bonds of each series shall be determined by the Authority by and in the resolution establishing such series, and that the resolution establishing any series may contain other terms and provisions not inconsistent with the Consolidated Bond Resolution; and

WHEREAS, the Authority has heretofore established various series of said Consolidated Bonds and has now determined that it is necessary, advisable and in the public interest to establish another series of said Consolidated Bonds, without prejudice to its right hereafter to establish other and additional series of such Consolidated Bonds;

NOW, THEREFORE, be it resolved by The Port Authority of New York and New Jersey: (pp. 69-72)***.

SECTION 7. The Authority shall not apply any monies in the Consolidated Bond Reserve Fund or in any special reserve fund established for the benefit of the bonds of any prior issue of bonds except for the payment of bonds secured by a pledge of the General Reserve Fund in whole or in part, the payment of debt service upon bonds so secured, the purchase for retirement of bonds so secured or the redemption of bonds so secured, or for the payment of expenses incurred for the establishment, acquisition, construction or effectuation, or for the operation, maintenance, repair or administration of any facility financed or refi-

nanced in whole or in part by bonds secured by a pledge of the General Reserve Fund in whole or in part, or otherwise for the fulfillment of any undertakings which the Authority has assumed or may or shall hereafter assume to or for the benefit of the holders of bonds secured by a pledge of the General Reserve Fund in whole or in part; provided, however, that nothing herein contained shall be construed to permit the application by the Authority of monies in the Consolidated Bond Reserve Fund or in any special reserve fund established for the benefit of the bonds of any prior issue of bonds except for purposes and upon conditions which in the case of the Consolidated Bond Reserve Fund are authorized by the Consolidated Bond Resolution or in the case of said special reserve funds are authorized by the respective resolutions establishing such prior issues of bonds.

Consolidated Bonds proposed to be issued for purposes in connection with an additional facility or a group of additional facilities in connection with which the Authority has not theretofore issued bonds which have been secured by a pledge of the General Reserve Fund in whole or in part, may be issued, and bonds other than Consolidated Bonds proposed to be issued for purposes in connection with such an additional facility or group of additional facilities may be secured by a pledge of the General Reserve Fund in whole or in part, in each case if and only if the Authority shall certify at the time of issuance (as defined in Section 3 of the Consolidated Bond Resolution) its opinion that the issuance of such Consolidated Bonds or that such pledge of the General Reserve Fund as security for such bonds other than Consolidated Bonds will not, during the ensuing ten years or during the longest term of

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any of such bonds proposed to be issued (whether or not Consolidated Bonds), whichever shall be longer, in the light of its estimated expenditures in connection with such additional facility or such group of additional facilities, materially impair the sound credit standing of the Authority or the investment status of Consolidated Bonds or the ability of the Authority to fulfill its commitments, whether statutory or contractual or reasonably incidental thereto, including its undertakings to the holders of Consolidated Bonds; and the Authority may apply monies in the General Reserve Fund for purposes in connection with those of its bonds and only those of its bonds which it has theretofore secured by a pledge of the General Reserve Fund in whole or in part. Expenditures in connection with an additional facility or group of additional facilities shall mean the amount of the excess, if any, of the sum of all items of expense to be considered in determining the net revenues of the additional facility or group of additional facilities plus the debt service upon the bonds proposed to be issued and upon any additional bonds which in the Authority's opinion would be required to be issued to place and maintain such facility or group of facilities upon a sound operating basis, over and above the sum of all items of revenue and income to be considered in determining such net revenues. (p. 76) • • •

Excerpts From Exhibit III to Stipulation Among Counsel Dated December 20, 1974

THE PORT AUTHORITY OF NY & NJ
1973 ANNUAL REPORT

• • •

"PLAINFIELD CORRIDOR SERVICE PROJECT

As authorized by the States in 1973, PATH began detailed planning for the Plainfield Corridor Service Project, an extension of PATH from Newark to Plainfield via Newark International Airport and Elizabeth, more than double the present mileage of PATH.

Primary goal of the PATH extension is the retention of rail service for approximately 8,000 riders of the Central Railroad of New Jersey (CNJ), whose rail service has been threatened with abandonment. The proposed extended service also would include a new station stop at McClellan Street, Newark, to provide rail service to Newark International Airport.

As part of this extension, a new rail line would be constructed alongside the Penn Central tracks between Penn Station-Newark and Elizabeth, including the airport station at McClellan Street.

Basic system and structural improvements would be required along the CNJ right-of-way between Elizabeth and Plainfield, including station construction at Elizabeth, Roselle/Roselle Park, Cranford, Westfield/Garwood, Fanwood/Scotch Plains and Plainfield.

Forty-four new rapid transit cars would be purchased by PATH and many existing cars would be extensively refurbished for the service. Other equipment for track, signal and power systems also would be required.

The estimated gross cost of the Plainfield Corridor Service Project is $221,510,000, toward which an 80 percent capital grant would be required under the Federal Urban

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Mass Transportation Program. A preliminary grant application was filed in October, and public hearings called for by UMTA, the responsible Federal agency, were scheduled for January 1974.

The local share would be provided by the Port Authority and, to the extent necessary, the State of New Jersey.

The PATH extension would relieve the taxpayers of the State of New Jersey of the present operating subsidy obligations for CNJ passenger service in the area served and of the responsibility for capital improvement programs which had been identified for the CNJ in the Corridor.

Detailed planning and community contact work were under way throughout the year. Through meetings with community officials, planners and trade and civic leaders, every effort was made to acquire data and encourage citizen participation in the planning process.

"Penn Station Direct Access

The Plainfield Corridor Service Project is one element in a three-part metropolitan area rail transportation improvement program delegated to the Port Authority. The second is a project to provide rail service to Kennedy International Airport (see page 27). The third is the Penn Station Direct Access Project, which calls for rail connections and station improvements at Penn Station-New York to permit operation of Erie Lackawanna trains directly into New York City.

Track connections between the Penn Central and Erie Lackawanna railways in Kearney and Secaucus will permit selected Erie Lackawanna trains, carrying some 20,000 riders, to travel directly into Manhattan from areas in northern New Jersey and upstate New York. The project also includes construction of a new high-level Penn Central

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bridge over the Hackensack River and construction of yard facilities in New Jersey.

Detailed design work has been in process on the Penn Station Direct Rail Access Project throughout the year. Consultants are undertaking computer simulations of the train movements into and out of Penn Station to reach detailed engineering design decisions. They also are studying power, signal systems and communications improvements included in the plan." (pp. 12-15).***

Excerpts from Exhibit III to Stipulation Among Counsel Dated December 20, 1974

SELECTED FINANCIAL DATA

	1973
Net Revenues	
Gross Operating Revenues	$ 373,497
Operating Expenses	236,434
Net Operating Revenues	137,063
Other Income	23,615
Net Revenues Before Debt Service	160,678
Interest on Bonded Debt	49,729
Balance Available for Debt Retirement and Reserves	110,949
Times, Interest Earned	3.23
Mandatory Long-Term Debt Retirements	26,047
Net Revenues after Debt Service	$ 84,902
Times, Debt Service Earned	2.12
Net Changes in Reserves	
Transferred from Revenues (above)	$ 84,902
Interest on Bank Loans	(6,775)
Bank Loan Payment	(35,000)
Short-Term Note Retirements	—
Long-Term Debt Retirement Acceleration	—
Invested in Facilities	(8,000)
Debt Service on Bonds Secured by Trusts	(6,874)
Adjustment of Securities Value	(3,591)
Net Change	$ 24,662

Excerpts from Exhibit III to Stipulation Among Counsel Dated December 20, 1974

	1973
Reserves—at Year End	
General Reserve	$ 173,487
Special Reserve	16,047
Air Terminal Reserve	22,664
Marine Terminal Reserve	2,634
Consolidated Bond Reserve	21,932
Total	$ 236,764
Dept—At Year End	
General and Refunding Bonds	$ 14,586
Air Terminal Bonds	20,577
Marine Terminal Bonds	2,417
Consolidated Bonds and Notes	1,697,287
Total Bonded Debt	1,734,867
Bank Loans	295,000
Total	$2,029,867
Invested in Facilities—At Year End	$3,272,913
Debt Retirement Through Revenues and Reserves	
Annually	$ 66,943
Cumulative	$1,261,357

(p. 71) • • •

Exhibit V to Stipulation Among Counsel
Dated December 20, 1974

A History of
THE PORT OF NEW YORK AUTHORITY
Financial Structure

taken from
an extemporaneous talk
By Daniel B. Goldberg
General Solicitor of the Port Authority

before
the executive staff of
The Port of New York Authority
October 3, 1961

Published April 1964

Introduction

At the time this talk was given in 1961, the Port Authority was about to enter a new phase of its financial history. Our organization was about to be asked by the Legislatures and Governors of the two States to assume responsibility for the bankrupt Hudson and Manhattan Railroad—a completely new kind of facility and one which we were convinced would never become self-supporting—without impairing our credit standing.

As the Port Authority's brilliant General Solicitor, Mr. Goldberg has played a key role, if not *the* key role, in the development of the Authority's present financial structure. He has also helped to build and protect the Authority's enviably sound fiscal integrity upon which our future rests. And he served as the chief architect of those financial safeguards, described in this talk, which made it possible the following year for us to assume responsibility for the H&M with adequate financial safeguards. His talk therefore has historical value in itself as well as being a lively and lucid explanation of how our financial structure grew over the years and how it works today.

A History of the Port Authority's Financial Structure

I'm going to start with an historical approach, because the history of the Port Authority's financing is almost a history of the Port Authority itself. Engineers built bridges and airports, and plans were made and the reports were promoted and developed before the Port Authority came along, but the innovation which the Port Authority represents, aside from interstate cooperation, is its legal and financial mechanism. So, let's go back in time to 1926 when the Port Authority put out its first bonds—its Series A bonds to construct the Arthur Kill bridges. The patterns of those bonds and of the Series B bonds for the George Washington Bridge and of the Series C bonds for the Bayonne Bridge were the same, so we can group them all together and this we can call Phase I.

Phase I

Closed End Bonds

The important point that distinguishes those first bonds from most that came along later was that they were not open-end bonds; they were closed-end bonds. An estimate was made of how much money it was going to take to build each bridge and that is the amount of the bonds which was authorized. We might borrow it all at one time—or at two times as in the case of the George Washington Bridge—but basically, we could not thereafter sell any more than the originally stipulated dollar amount for the originally identified facility. Those early bond issues were therefore closed-end issues.

The Series A bonds for the Arthur Kill bridges, the Series B bonds for the George Washington Bridge and the Series C bonds for the Bayonne Bridge had an identical pattern of application of gross revenues, which you can think of as the revenue flow. To trace the revenue flow in those early days, we start with the gross revenues coming in from the operation of each of the bridges. These were to be applied first to the expenses of operation and maintenance—O&M as we call it—of that bridge. Then the balance left in the case of each bridge was to be applied to debt service on the particular series of bonds which financed that particular bridge.

Now for those who are uninitiated in these "mysteries," debt service really means the same thing you pay as you make monthly payments on the mortgage on your home—it is a combination of interest and amortization of the principal of your loan. Debt service in the cases of our early closed-end bonds consisted of the interest on the bonds and some sinking fund requirements which were supposed to take care of repaying the principal. The setup then called for surplus revenues of each bridge after debt service on its particular bonds to go into separate statutory reserve funds, each of which was set up in the statute which authorized the financing of the particular bridge.

I needn't tell you that in fact there wasn't any surplus to take care of this statutory reserve. There was difficulty in meeting the debt service on those early bonds when the traffic estimates turned out to be more than the lean 1929-31 depression years produced.

Phase II

The second phase was the phase in which the walls between the individual facility revenue flows and the

individual bond issues turned out to be Walls of Jericho and fell down at the blast of the trumpet of the General Reserve Fund Statutes. In the early financial-legal structure, there was no way for any surplus, if it *had* been cleared by any one of the bridges, to have been used to supplement the revenue flow of any other facility which turned out to be a weak sister needing help to meet the demands under its bond indenture.

And so in 1931 the second phase of the Port Authority's financing began. I looked up some dates this morning and I found that the statute authorizing the General Reserve Fund was adopted on March 5, 1931, and the Port Authority had it pledged on March 9. It only took four days to use the new statutory authorization.

The first use was in connection with new Series D bonds and new Series E bonds. Series D bonds were to finance this Inland Terminal Building in which we now sit. The E bonds were to pay the two States the $50 million which they had spent to construct the Holland Tunnel, and for which the States were to turn over to the Port Authority the control of the revenues and operation of the Holland Tunnel. These two bond series provided pretty much the same pattern of revenue flow which I outlined for the older bonds, but there was a big new addition. And the big new addition was the General Reserve Fund.

General Reserve Fund

The General Reserve Fund is the absolute foundation of the Port Authority's whole financial structure. It is what made possible practically every advance after the first faltering steps in the initiation of our financial program with the first bridges. What we have had since 1931 is a statute which directs the Port Authority to pool the

revenues of all its facilities and, having pooled them, to use —and to pledge in advance if necessary—the surplus revenues that each facility or group of facilities might produce after it had met the requirements of the revenue flow of its particular bonds, so as to cross the fallen "Walls of Jericho" and to meet the requirements of any financially weak facility which had not yet reached its stride or which for any other reason could not at a particular point of time carry its own load of O&M and debt service.

The General Reserve Fund has an upper limit. Surplus revenues must be paid into it to maintain it at an amount equal to ten per cent of the principal amount of bonds issued to finance Port Authority facilities.

At the time in 1931 when this structure was worked out, the Holland Tunnel was an established facility with revenues in excess of the requirements directly related to it. As you know, it was built by a pair of state agencies working together. When the two States turned it over to the Port Authority in 1931, it was known that from this time on, after the flow of money through operation, maintenance and debt service, a surplus would be produced from the Holland Tunnel which would flow into the General Reserve Fund, and that this surplus in the Fund could be used to flow back up and take care of any deficits which we might have between the revenues of the other facilities and the debt service on the particular bonds issued to finance them.

The Series D bonds, which I mentioned as being to finance the construction of this building, and the Series E bonds for the Holland Tunnel acquisition were sold as a package. You had to buy one to get the other.

So Phase II includes for the first time, beginning with 1931, the Port Authority's ability to use the surplus funds

of any facility that produced surplus funds to meet what the statutes called obligations to bondholders.

BONDHOLDERS' RESERVE

I want to make it clear that the General Reserve Fund is not a grab bag. It is not a pot to be collected for the States to dip into, as they might be impelled from time to time by political or other motivation. The General Reserve Fund, under the statutes, is exclusively a *bondholders' reserve*. It gets the surplus revenues each year which the facilities produce, beyond the requirements to bondholders, and it may be applied only to fulfill obligations to bondholders. Since we covenant with bondholders, in the case of each of our facilities, to operate and maintain them so as to produce revenues and also to pay the debt service—the principal, the interest, the sinking fund payments—on the bonds, the General Reserve Fund is available for O&M and debt service purposes. But, as I say, it is not a source for "dividend" payments to the States. The bondholders, for a modest interest payment, took the risk of insufficient revenues in lean years and accepted the absence of recourse to taxes; but they very naturally insisted that the fruits of any years of plenty remain available for the lean years which might come with depression or with war and gasoline rationing, with uninsurable catastrophes or simply because of over-optimistic estimates.

Now this was about the time, you'll remember, when the two States were also projecting the construction of the Lincoln Tunnel. The transfer to the Port Authority of the Holland Tunnel in 1931, with its obvious surplus revenues, was supposed to be the basis of our having a surplus with which to attract money from private investment sources for building the Lincoln Tunnel.

By the time 1931 closed, the Port Authority's financial structure was as follows: We had five facilities, we had five bond issues, we had five revenue flows, and we had the General Reserve Fund. The Holland Tunnel was producing surpluses beyond the requirements of Series E bonds while the General Reserve Fund, by means of the surpluses from the Holland Tunnel, was in a position to meet the deficits on requirements for the other bond issues. And we were exploring ways to finance the proposed new Lincoln Tunnel.

Phase III

The financial structure then had become quite complicated, and it was apparent that it ought to be simplified. So this is the time when we come to the General and Refunding phase for the Port Authority—what we'll call Phase III.

General and Refunding Bond Program

When the new program was started in 1935, the idea was to replace all of the earlier bonds by refunding them with the new type of bonds, General and Refunding (or G&R), and also to finance the construction of the Lincoln Tunnel by such new bonds.

There were other purposes for which the General and Refunding bonds were permitted, but they were quite limited and I'll refer to them a bit later.

At any rate, with the initiation of the General and Refunding bond issue, in time all of these earlier bonds—Series A, B, C, D, and E—were refunded, replaced with General and Refunding bonds. Also, we financed the Lincoln Tunnel with G&R bonds as was expected; we financed the Grain Terminal, or at any rate we repaid the State advance which came with the Grain Terminal from the State of New York and financed its improvement; we

financed our two Truck Terminals and our Midtown Bus Terminal; and we initiated capital improvements to the earlier existing facilities.

The General and Refunding bond structure is not ancient history as the earlier ones are. There are bonds of the General and Refunding bond issue still outstanding, and as long as these bonds are outstanding the Port Authority is bound by the contracts with those bondholders. And they're significant, too, in limiting us in the otherwise available use of our revenues.

Special Reserve Fund

The revenue flow in the case of the General and Refunding bonds now involved a pot of pooled revenues. The big Walls of Jericho between each separate facility were now down. We now had the money from all the facilities we owned at the time, including the Lincoln Tunnel, in a pooled G&R facilities revenue flow structure. These pooled revenues would be used first for operation and maintenance on all G&R facilities; then for debt service on the G&R bonds; and then put into a new contractual Special Reserve Fund which substituted for the various previous independent statutory reserve funds for each of the early Series A, B, and C bond issues.

What the States found was that in the earlier structure, the statutory reserve funds for each early issue which were to receive a fixed schedule of amounts set up in advance called for more than the Port Authority was able to meet. So when the General and Refunding bond program was initiated, it was felt that the amount of the equivalent reserve fund should be an elastic figure. The way it was worked out was that the Port Authority agreed with the bondholders that we would apply the monies for all of these

G&R facilities in this order: first operation and maintenance on all the facilities, then debt service on all the G&R bonds, then we would pay into the new Special Reserve Fund all of the remaining net revenues except those necessary to keep the General Reserve Fund at the 10 per cent figure.

We would use, as needed, all the revenues for operation and maintenance; as needed, all the remaining revenues for debt service; as needed, all the still remaining revenues to bring the General Reserve Fund up to the 10 per cent figure. But all the ultimate remaining balance would have to go into the Special Reserve Fund.

The General Reserve Fund didn't reach its upper-dollar limit of 10 per cent of the par value of the outstanding bonds for fifteen years. It first reached that figure at the end of 1946. But from 1946 to date the General Reserve Fund has always been full and payments could then be made into the Special Reserve Fund. Of course, the 10 per cent figure changes from year to year as the amount of the bonds goes up, or down. To date, it always has gone up at each year end.

Now this is lesson number one in the Port Authority's bond structure: There are no "free monies" in the Port Authority's bond structure; there is no pot of gold into which anyone can dip. The General Reserve Fund, as has been mentioned before, may be used only to fulfill obligations to bondholders—and basically again that means: operation and maintenance, debt service, and some capital expenditures that might be necessary within limitations.

The Special Reserve Fund which is created by contract with the General and Refunding bondholders has a similar limitation on it. We may use the Special Reserve Fund monies, obviously, for operating the General and Refunding bond facilities if any one of them might actually have

an operating deficit—I don't think that's been so, in fact. We can use them for various purposes like buying General and Refunding bonds in the open market to retire them, payments into sinking funds on General and Refunding bonds and other purposes relating to the payment of interest on and the retirement—even accelerated retirement—of the General and Refunding bonds.

Then there is a final provision in our agreement with regard to the Special Reserve Fund that we might use a certain amount (which is 50 per cent of the aggregate payments into the Fund) for certain other purposes. This has led to the belief in some quarters that the Port Authority has a residue of monies that is not pledged to bondholders. That is not the case.

The entire agreement with Port Authority General and Refunding bondholders is that the Special Reserve Fund must be used for purposes which will enhance or maintain the security of General and Refunding bonds. Since each facility whose revenue flow can end up in the General Reserve Fund can support each other such facility, the Special Reserve Fund monies need not necessarily be used only for General and Refunding bond facilities—you'll notice that at this point in our narrative we don't yet have air terminals in the picture and among marine terminals, only the Grain Terminal. So although, because of the interdependence of all General Reserve Fund facilities, the balances in the Special Reserve Funds which are not going to be used for General and Refunding bonds and their related facilities may cross over the line of the General and Refunding bond facilities, still they never can get out of the total General Reserve Fund family of facilities—which we can look upon at the present time as all Port Authority facilities.

There is no pot of loose gold in the case of the Port Authority. All revenues have been pledged and all reserves have been pledged.

As I have said, the purposes for which the General and Refunding bonds could be used were quite limited. They could be used for refunding, as they were to retire the old Series A, B, C, D, and E bonds. They could be used, and were used, to finance the Lincoln Tunnel. They could be used to *refund* bonds issued to start new facilities but could not themselves be used to start them. That means that if you could start a new facility by using not General and Refunding bonds but some bonds like the old Series A, B, C, D, and E bonds, you could refund them, with some strict roll-over tests, with General and Refunding bonds; but this presented you with the problem of how you were going to finance them in the first place if you didn't have the General Reserve Fund behind the special purpose bonds.

And then there was a limited $15 million of General and Refunding bonds which could be used for new facilities—not over $5 million for an individual facility. Now you know how far $15 million for a group of facilities or $5 million for a new facility would go in the post-war construction market. Capital improvements could be financed by General and Refunding bonds with very severe limitations. And then there was a meager $8½ million of possible G&R bonds we didn't have to do very much about justifying.

Phase IV

And so when in 1947 the Port Authority was confronted with the necessity of financing airports, it was obvious that the General and Refunding bond structure was absolutely unsuitable and could not work. So Phase IV of the Port Authority's financial history came into being. It was a

period during which we pretty much duplicated the General and Refunding bond revenue flow for a new issue of Air Terminal bonds, which could be issued only for air terminal purposes, and then we set up Marine Terminal bonds which again duplicated the flow for projected marine terminals.

We now had Air Terminal and Marine Terminal bonds as well as G&R bonds. We now had three separate families of facilities and bonds, each with a similar pattern, with the General Reserve Fund back of all of them and the ability to take the surplus revenues produced by each family of facilities and feed them back in to meet the shortages that either of the other two families was going to have. It was obvious when we started with the air terminals that they were not going to carry their own weight in the opening years of our management of them—so that the by now more than self-supporting G&R family, which included bridges and tunnels, would be able to contribute surpluses which we needed to support the Air Terminal Bonds and Marine Terminal Bonds in their earlier years.

Remember, however, that the way in which the George Washington Bridge, for example, could contribute surpluses to Newark Airport purposes was through the mechanism of the General Reserve Fund. George Washington Bridge revenues, along with the revenues of all other G&R facilities, were first applied to O&M of this group of facilities, then to G&R bond debt service, then to the Special Reserve Fund for G&R Bonds, and finally to the General Reserve Fund. As General Reserve Fund money, it could then be used to fulfill obligations to the holders of Air Terminal Bonds to operate Newark Airport and pay any debt service on Air Terminal Bonds which the Air Terminal group of facilities couldn't meet by itself.

Therefore, in setting up the Air Terminal Bonds and Marine Terminal Bonds, it was necessary to assure their

prospective purchasers that the General Reserve Fund was not going to be depleted in any untoward way. And so we evolved the two years' debt service resolution of November 13, 1947—which, unfortunately, is one of the most misunderstood parts of P.A. financial policy.

There are two sets of teeth in the two years' debt service resolution. One set restricts the purposes to which the General Reserve Fund may be applied. The second set establishes how the General Reserve Fund monies shall be invested. Neither set *requires*—as is so often misstated—that the General Reserve Fund shall at all times have in it an amount equal to the next two years' debt service. Such a restriction would defeat the purpose of a reserve fund which is to be available to be *used* in a financial emergency, even if the use brings the balance below a desirable figure.

Actually the resolution imposed no new limitations on the Port Authority's power to use that portion of the General Reserve Fund which represented an excess in all combined debt reserve funds (General and various special reserve funds) over the next two years' debt service at the time. But except for that excess over the next two years' debt service, the monies in the General Reserve Fund could no longer be used for accelerated debt retirement or for any other purpose for which there might be other funds available at the time.

Similarly, the amount in excess of the next two years' debt service could be invested subject to the ordinary governing contractual limitations—i.e., principally in the P.A.'s own bonds. But the amount up to the two years' debt service figure could now be invested only in U.S. Government bonds, or kept as cash on deposit.

This program of voluntary self-limitation helped to establish a favorable climate for Air Terminal bonds and

Marine Terminal bonds. By once again assuring the inviolability of the General Reserve Fund, it strengthened the basic security of these new bond issues until the new facilities on whose revenues they had a first lien should become self-supporting in their own right.

However, with three families of facilities and three related bond issues, we were getting to duplicate on a larger scale the original structure we had with our Series A, B, and C bonds; our structure was getting unwieldy again. So that by 1952, the need was felt to revise the bond structure once more, pretty much along the lines of the need we had felt around 1935 to have the streamlining of the General and Refunding bond issue.

Phase V

The motivation was partly streamlining and partly the fact that we were getting ourselves into a situation where we really didn't have any type of bond that we could put out except for a limited purpose. Air Terminal bonds were available only for air terminals, and Marine Terminal bonds for marine terminals; General and Refunding bonds, with their limitations of $5 million per project and $8½ million free, just didn't fit the cost pattern of the post-war age. And so in 1952 we set out to develop an entirely new streamlined bond structure—and that is the one that we're living with now.

Consolidated Bonds

We are now in Phase V, the Consolidated Bonds phase. The first thing we did was to provide that these bonds could be issued for unlimited purposes, that is, any purposes that The Port of New York Authority was authorized by statute to go forward with and to use the General Reserve Fund

in connection with. In the second place we came to the problem of the closed bond versus the open-end bond. The Consolidated Bonds, like the General and Refunding Air Terminal and Marine Terminal bonds before them, are an open-end bond. That is to say, there is no dollar amount which limits the amount of them that the Port Authority can issue. In the case of the General and Refunding bonds, the open-end feature had become more theoretical than real because the purposes were so limited; these small dollar limits on the amounts that we could put out to construct new facilities practically made G&R bonds only Lincoln Tunnel bonds or improvement bonds for existing facilities, or refunding bonds.

But as we came to draft the Consolidated Bond structure, we looked forward to the enormous post-war horizons that the Port Authority was facing up to. We needed a new financial device where the purposes would be unlimited, where the dollars would be unlimited, and only legality and financial practicability would impose the limits. You know that our financial program today calls for something like a billion dollars of new capital money to be raised over the next ten years. As of 1952, adding what we've done between that time and now, and what we have left to do, the figures were and are astronomical.

The holder of a Port Authority bond has nothing to look to for the repayment of the principal and interest on his bond except the revenues that the Port Authority can derive from the facilities in a particular year and except for the reserves in which it can impound them—the special reserves and general reserve—from year to year. And so he has to know at any point of time, when he lends us his good money—or the money of beneficiaries of trusts he administers—he has to know that there is not only a good prospect but almost a certainty, as far as those things can be calculated, that he is going to be paid back.

And so he must be sure that the Port Authority is not able to dilute the net revenue potential of the facilities to a point where the money that is going to come in—this gross revenue box that we start off with at the head of each column in the revenue flow chart—is going to get too small for the O&M and the debt service that it has to cover. He wants to be sure that we don't balloon the amount of our bonds up so big and get our debt service up so big and, in the case of a facility w'ch wouldn't be carrying itself, like a Hudson & Manhattan Railroad, even get its operation and maintenance expenses up so big, that there wouldn't be enough over-all to meet the debt service on his bonds and on the new bonds that might be put out in connection with new facilities.

1.3 Earnings Test

Now the mechanism by which this insurance was given was the 1.3 earnings test. All this test is is a requirement that the Port Authority will not issue new Consolidated Bonds unless it can show, at each point of time it proposes to issue new consolidated bonds, that certain earnings equal 130 per cent of, or 1.3 times certain debt service on certain bonds. For the most part, the earnings that are used in this equation are historical earnings. They are the best twelve months out of the previous thirty-six months and in practice these have always been the last year, which has always been our best year. In certain limited instances we can augment these historical earnings with some estimates, but for the most part you can think of the earnings that we have to use in this test as historical earnings.

On the other side of the equation is the debt service—that is the interest, the amortization on the bonds, the

annual maturities, the sinking fund requirements—which we must cover 1.3 times out of these earnings. This debt service is the requirement for that year in the future when our scheduled debt service will be at a maximum. In other words, we must take our peak demand year in the future for combined debt service on already-issued bonds and the proposed new bonds. We know our scheduled sinking fund and principal maturities; we know our scheduled interest requirements. We look up the schedule to figure out in which year in the future our scheduled debt service will be the heaviest, and then we compare this with our historical earnings, and if we can't show that the maximum future year's debt service requirements have been met historically in one of the past three years 1.3 times, we can't issue a Consolidated Bond.

For all practical purposes, that means we can't finance at all at that time. Theoretically, if a proposed new facility could be self-supporting, we might be able to work a financing like the old Series A, B, C, D, and E bonds without using Consolidated Bonds. But the things that the States direct the Port Authority to do these days are not capable of immediate self-support. So we are practically restricted to Consolidated Bonds, and that means we must satisfy the 1.3 earnings test.

We do have alternates in applying this 1.3 earnings test. First, we can meet it on a proposed new facility by itself. In other words, if a new facility which the Port Authority proposed to buy had historical earnings which were 1.3 times the debt service on the bonds we were proposing to put out to buy it, then even if every other facility was in financial trouble at the time, we could put Consolidated Bonds out to buy the new one because this would not dilute an existing coverage and the new facility would be carrying its own weight 1.3 times. This is a most unlikely situation, but it is provided for.

We have another alternate under which we can apply this 1.3 earnings test across the family of Consolidated Bond facilities. Now, the family of Consolidated Bond facilities consists of all those facilities which were financed only with Consolidated Bonds and not with the Series A, B, C, D, E, G&R, Air Terminal or Marine Terminal bonds. At the moment this family consists of the Hoboken, Elizabeth, Brooklyn, and Erie Basin Piers, and the two heliports. New facilities so financed would be added—such as the Hudson Tubes, and the new World Trade Center. If that family of facilities could show historical earnings 1.3 times the maximum future debt service requirements on all Consolidated Bonds, including those new ones proposed to be issued, we could put new Consolidated Bonds out to acquire a new Consolidated Bond facility that would be in that family. This alternative is not likely to happen for some years.

The real test, under which we have, in fact, done all of our Consolidated Bond financing to date, is the third test. This measures the financial picture of the entire group of Port Authority facilities—we call it the General Reserve Fund family because at the present time, aside from the commuter car program, every single Port Authority facility can legally contribute to and be supported by the General Reserve Fund.

Under this test, if we want to put out a new Consolidated Bond series, we must show as a practical matter that the historical earnings of all Port Authority facilities will cover at least 1.3 times the debt service we will have on all new bonds in that year in the future when our debt service will be at a maximum. Now that is a rigorous

requirement. We have met it easily in the past. But the entire program on which we are embarking contemplates that the coverages that we have produced will come down closer to the 1.3 times test figure—although never really near it, I hope, because with us 1.3 is absolute zero. At the point where we can only show barely 1.3 or a whisker under 1.3, we can't put out Consolidated Bonds. The 1.3 status is not prosperity to us; it is practically the point of enforced stagnation. It is the point at which our ability to finance any future projects, even any capital improvements to existing facilities, ceases. For the Port Authority to continue as a healthy, vigorous organization, doing the job it was set up to do and which it has done so well in the past, we must keep our coverages up as high as we can.

In order to issue our Consolidated Bonds in the first instance, it was necessary, of course, for us to close our General and Refunding bond, our Air Terminal bond, and our Marine Terminal bond issues. This was because it was from the surpluses to be produced by the existing facilities over the debt service on the old-line bonds that we were going to cover the debt service requirements on the Consolidated Bonds for years to come. If we were able to continue to put out increasing amounts of General and Refunding bonds, the Consolidated bondholder would have no certainty that any surplus revenues would be available for his bonds. So when we initiated the Consolidated Bond issue, we agreed with the Consolidated bondholders that we would no longer put out General and Refunding, or Air Terminal, or Marine Terminal bonds.

Revenue Flow

At the present time, then, the revenue flow in the case of Port Authority facilities is of two kinds. The existing flows

that we had for the old-line bonds still remain. The General and Refunding bond flow remains as long as there are any G&R bonds outstanding; the latest present maturity dates are well into the 1980's. And similarly, Air Terminal and Marine Terminal bonds flows will continue as long as any of those bonds remain outstanding. In addition, we have the flow for the new Consolidated Bond family.

Since 1952, we have used Consolidated Bonds as the sole medium of general financing. We've used them not only for financing the newer facilities—the Hoboken, Elizabeth, Brooklyn and Erie Basin Piers and the Heliports—but also for all the major capital improvements to the pre-existing facilities. We've used Consolidated Bonds to finance the Lincoln Tunnel Third Tube, the GWB Second Deck, NYIA enlargements, LaGuardia rehabilitation and everything else that we have done in the last nine years.

From the point of view of revenue flow, what is actually happening now is that these three older families of facilities —General and Refunding, Air Terminal, and Marine Terminal—are now covering their operation and maintenance, their debt service and their requirements to keep the General Reserve Fund full, with something left over for the three Special Reserve Funds; whereas the new Consolidated Bond facilities, if we thought of them as having to meet solely from their own revenues the debt service on *all* Consolidated Bonds, are deeply in the red.

Of course, this theoretical deficit had to be because the Second Deck of the GWB has been financed through Consolidated Bonds and yet *all* of the George Washington Bridge revenues must go into the G&R revenue flow line; the huge NYIA expansion program has been financed in large part with Consolidated Bonds, but all the revenues thus generated must go into the Air Terminal revenue flow line.

Exhibit V to Stipulation Among Counsel
Dated December 20, 1974

As a result, what we really have are downward flows from the old-line facilities into the General Reserve Fund and the Special Reserve Funds, and then a reverse flow back-up to take care of requirements for the Consolidated Bond facilities—to cover any O&M shortage and the shortage on debt service which must exist as long as the old-line bonds remain outstanding. At long last, sometime in the future, when all of these old-line bonds are retired, there will be only one revenue flow. All the facilities will then be in the enlarged Consolidated Bond family of facilities and their revenues will cover directly all related debt service.

The proposals that we be directed to take over railroad operations in both States would involve, without the New York subway system, something like $30 million of operating losses plus the debt service on bonds that we might have to issue to acquire the properties which produce this headache. These proposals made us take a good look at our financial structure to see to what extent, if at all, we were open to this kind of a financial raid at the sacrifice of the security that our bondholders had bargained for when they had loaned us hundreds of millions of dollars.

We actually found, as I have tried to indicate, that there was no hole in the structure, there was no pot of gold into which to dip. *All* the revenues were pledged to particular families of bonds; *all* of them had to be used either to pay the operating and maintenance expenses of the particular facilities or the debt service on particular bonds, or to keep the General Reserve Fund full, or for the Special Reserve Funds—and the Reserve Funds themselves were available only for things which would maintain or enhance the security of the bonds.

Certainly you could not make the claim that Reserve Fund expenditures would maintain or enhance the security

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of our bonds if the money was to go outside of the P.A. family of facilities, as was proposed in one suggestion that we simply subsidize the private railroads to the extent of their commuter operating deficits.

However there still was a fear in the financial community that the Port Authority might somehow take *into* its General Reserve Fund family a group of deficit-ridden railroads and then, by having gotten the disease into our own financial body, be in a position legally to apply our monies to their operating and debt service deficits. The fear was that in some such way we might actually dilute our earning and reserve position to a point where we would no longer have the financial capacity to meet the requirements of the existing bonds and of any other bonds we might have to put out for our self-supporting projects.

We in the Law Department have always held the firm opinion that Port Authority *lacks* the power so to dilute the security of its bondholders, and we have advised the Commissioners to that effect. It would be just as ludicrous, to us, to suggest that the Port Authority could accept the New York City public school system as a gift and then, it being in our family of facilities, apply all of our revenues to paying teachers' salaries so there wouldn't be anything left to pay the principal and interest on our bonds. We knew we couldn't do that. However, the fears of the financial community were real, and so we felt that this legal opinion which we have should be codified in a form that would be not only a legal opinion, which could be disputed, but a firm written contract. And so we proposed what we call our Section 7 certification. Ever since the 12th series of our Consolidated Bonds, we have had in each series an agreement with our bondholders that we would not take on a new facility except under circumstances where our Commissioners could certify in good faith that it would not

Exhibit V to Stipulation Among Counsel
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unduly impair the sound credit standing of the Port Authority or the investment status of Consolidated Bonds. To us, this was merely a contractual codification of an agreement and obligation which we had anyhow, but it has helped to allay the fears of the financial community.

As for the future? I don't know . . . but I think you will see there is an intimate connection in Port Authority history between the financial structure and the direction we take.

The differences during 1961 between the State of New York and the State of New Jersey as to how the P.A. can provide some help in solving the railroad commuter problem have been for the most part differences as to the assurances which would be given to our bondholders. The statute which was first passed in the State of New York on the subject of the H&M also included the proposed World Trade Center. But our principal problem with that statute was that it did not provide certain assurances to bondholders which we considered essential to making the sound credit standing certifications that I described, and to holding the P.A.'s credit together and doing the job. The bill in New Jersey, which never was enacted, first started in that direction . . . but it too had some faults. The two States have not resolved their differences—and I hope they will. We're doing our best to bring them together but the only way in which they can successfully come together and keep the P.A. functioning as a worthwhile legal-financial institution is by giving our bondholders the assurances which they need for us to continue financing as we try to do the job*

* Since Mr. Goldberg presented this summary, the two States have reached agreement along the lines he discussed and the Hudson Tubes-World Trade Center legislation of 1962 contains adequate assurances to bondholders.

Exhibit V to Stipulation Among Counsel
Dated December 20, 1974

Question by Mr. Tobin: "You might tell us more about the statutory assurances needed in any H&M legislation."

Mr. Goldberg: The assurances which we have suggested be placed in the statutes which would authorize us to do the H&M job are, as we propose them, in the form of an actual contract between the two States and the holders of our bonds. Contracts of this type can be made and cannot be breached by subsequent legislatures. This is because the Constitution of the United States says that no State shall impair the obligations of a contract. It is our opinion, concurred in by our present bond counsel and by his predecessor, and not challenged by anyone, that the contract we propose, if inserted in the legislation, would be binding and would constitute an unbreachable contract by the States.

Now that contract would be an agreement that the P.A. would not be permitted or directed to apply its General Reserve Fund monies to a new commuter railroad after the H&M except under stated circumstances. (It is the General Reserve Fund that we're trying to protect here. If a proposal can be done outside the General Reserve Fund structure, we don't have a problem of preserving credit.) The agreement would be that, before we put out bonds or in any way commit the General Reserve Fund to any application to the deficits of any commuter railroad facilities, the P.A. Commissioners would have to make a formal certification. The certification would be that the estimated deficits after operation and maintenance and debt service requirements of the proposed new commuter railroad facility would not exceed a certain figure. The figure may be thought of generally as one-tenth of the amount in the General Reserve Fund at the time, provided it is full.

Exhibit V to Stipulation Among Counsel
Dated December 20, 1974

At the present time, we have some $65 million in the General Reserve Fund, and it is full, which means we have a debt of some $650 million. Ten per cent of that $65 million—or $6½ million—would thus be the limiting figure at the present moment, if such a certification had to be made.

That $6½ million would be used in this way . . . after acquisition of the H&M. We have estimated that the H&M will drain from reserves about $5 million a year over and above its own revenue take—so that at the present there would be a margin of $1½ million between that $5 million estimated deficit and the $6½ million figure which is 10 per cent of the $65 million in the General Reserve Fund. As long as those figures prevailed, we could not take an additional commuter railroad into the General Reserve Fund family if its estimated annual deficits exceeded the $1½ million margin.

Now assuming an agreement between the two States which gets the H&M into the General Reserve Fund family —and assuming this covenant limiting inroads on the General Reserve Fund were enacted by the two States—suppose it were then proposed that we undertake the enlargement of the H&M, or maybe that we take over some additional commuter railroad facility. At that time, we would take whatever the established H&M deficit was, we'd project over the next ten years our estimate of what that deficit would average and then add our estimate of the projected ten year average deficit on the proposed new commuter railroad facility, and we'd have a total. On the other side of the test equation, we'd take 10 per cent of our then General Reserve Fund figure, and if 10 per cent of our General Reserve Fund figure would cover our estimated annual deficit on the now-grouped H&M plus additional commuter railroad facilities, we could take the proposed additional

Exhibit V to Stipulation Among Counsel
Dated December 20, 1974

facility into the General Reserve Fund family. Otherwise we couldn't.

After we first proposed this test formula, it was suggested that it was unduly rigid because, theoretically—or even actually, but not in the foreseeable future—our debt would some day decline and as our debt declined, the General Reserve Fund which is based on 10 per cent of the debt would also decline . . . and yet our revenues might not only remain constant but increase, so that our ability to take on commuter railroad facilities might be greater while our test figure was going down. We acknowledged this might eventuate and so we tried to meet that possibility by proposing an alternative under which the test figure based on one-tenth of our General Reserve Fund would be augmented by one per cent of our equity. By "equity" we meant debt retired from income or reserves. This covers a "someday and maybe" situation. It has been our final proposal. It is in the last draft of the bill which our office produced (and is part of the latest New Jersey bill to be introduced on the subject).

If enacted, it would produce a result which we could live with because, as we now know, the financial community will accept it. We know that to be so because we have canvassed critical investor opinion on the subject.*

* Final enactment along these lines was accomplished in 1962.

Excerpts from Testimony of John F. Thompson

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[2] Mr. Meyner: This is a hearing in order to procure testimony with reference to reliance and the effect on the secondary market by reason of the repeal of the 1962 covenant by the 1974 statute. T 2-16 to 2-20.

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[18] Q. What has been the nature of your employment with the Morton Company? A. I am vice-president. I am the head of a very small department which we call credit and finance. I have done a good deal of work of the firm in helping to structure new issues of some of the state agencies and authorities which the Morton Company is particularly a manager in the underwriting of.

I have also been responsible for describing and explaining credits of all sorts of municipal issues, not only to our salesmen but to customers of our salesmen both in conversation and in written memoranda which are circulated to both the salesmen and the customers.

[19] Q. Describe more specifically the operation of Morton and Company and your role in its operation. A. The Morton and Company is an underwriter and dealer specifically in municipal bonds. We do not have any other business at this time except for a small amount of Federal Agency sales on their new issues, but our specific business is municipal bonds.

In the underwriting of municipal bonds the Morton Company has what it called a major position in many of the syndicates which underwrite large issues. In quite a number the Morton Company is a manager of the syndicates. We have been a manager in part of Port Authority financing, the firm has in the period beginning 1964 and during the period 1967-1968 when the Port Authority issues were first increased to the size of $100 million each and sold. By

negotiation the Morton firm was one of four managing underwriters in the business.

We also deal in the secondary market, feeling that a good dealer is prepared to make markets in the issues which he has sold to customers, and also is prepared to buy holdings from a customer in the course of distributing in a new issue. The distribution of a new issue in the primary market and the purchase and sales in the secondary are often related in this way.

[20] Q. But what is the underwriting liability that Morton and Company undertakes? A. Last year we participated I believe in some four billion of new issues, and our underwriting liability was somewhere around 225 to 250 million in the course of the year.

Q. How many offices does Morton and Company have? A. The Morton and Company operates from just one office. We do a nationwide business but from one office.

Q. How would you characterize the nature of the customers dealt with by Morton and Company? A. The customers dealt with by our firm are largely what are known in the trade as institutional customers, by which we mean commercial banks, life insurance companies, trust departments of commercial banks, investment counsel firms, and the municipal bond funds. T 18-8 to 20-18.

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[21] Q. Have you been involved, Mr. Thompson, with any professional associations with regard to your operation? A. Yes, with quite a number. Early or after I came to Morton and Company I was put on the Investment Bankers Association Special Research, and spent a good deal of time in the ensuing year in working on the problem of defending the tax exempt market in the face of the drive for what was known as tax reform in Washington.

Excerpts from Testimony of John F. Thompson

And I am now Chairman of the Research Committee of the Public Finance Council of the Securities Industry Association, which is the successor to the old IBA or Investment Bankers Association.

I am a member and past President of the Society of Municipal Analysts, which is a nationwide group with some selected twenty-five or thirty members, professionals in the municipal bond business, particularly attuned to the credit side of the business.

I am a member and past President of the Municipal Forum of New York. I for a considerable number of years [22] was a member of the former Mayor Lindsay's Fiscal Advisory Committee, and I was a member of the Twentieth Century Fund Task Force that did a study of the rating agencies and the rating problem which eventually was published under the title of the rating.

Q. Did that latter publication cover municipal bond ratings or only corporate bond ratings, or both? A. Solely municipal bond ratings.

Mr. Landis: I submit Mr. Thompson as an expert and offer him for cross-examination on his expertise.

Mr. Sovern: We have no question.

The Court: You may proceed. T 21-6 to 22-13.

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[26] Q. What are the different types of municipal bonds that are commonly dealt with? A. Well, classification is done in varying ways in different places, but I think we can say that they are principally four types.

First is the general obligation tax-supported bonds, such as the general obligation of the State of New Jersey [27] or the State of New York or the City of New York, or of any of the cities here.

Excerpts from Testimony of John F. Thompson

The second type of obligation is a special obligation payable only from certain specific taxes. Some states have issued highway bonds payable solely from the proceeds of highway revenues which include the gasoline and motor vehicle taxes.

The third type, and this is the type in which the Port Authority bonds fall, is the revenue bonds payable solely from revenues received from the projects operated by either the Authority or the municipality, if it's water revenue bonds issued by a municipality and so on.

There's a fourth group that has come into prominence in the last few years. They are in part at least revenue bonds. That is, there is a revenue source and a flow of funds provided for the bonds but it was felt in issuing them that some stronger security should be given and a device was set up in which a reserve fund was established either by the issuing bond or by—from the proceeds of the bond equal to one year's interest and principal payment.

Then the state of issuance, these are largely state obligations. The state of issuance, by statute, provided that the state should reimburse the reserve fund if it had to be drawn upon in case other funds were inadequate to pay principal and interest.

[28] One can call these reserve makeup clause bonds. In the market, they are commonly called moral obligations. This is a term which has some disadvantages but it is a term that is generally used to describe this type of bond.

Principally, because the State as such cannot be compelled to restore the balance in the reserve fund, but has indicated through legislation that it will in case of need.

Q. Are they— these latter category of bonds, are they common in the states of New York and New Jersey? A. Yes. They started in the state of New York and there must be, oh, at least five billion bonds of that sort outstand-

ing in the state of New York, perhaps a little more now. They started with the Housing Finance Agency. The same reserve provision was given to the Urban Development Corporation, the Battery Park City Authority and I believe some others.

In the state of New Jersey there is this sort of a provision in the New Jersey Mortgage Authority or Housing Authority, whichever it is called here, that is an agency to assist in the mortgage market. This feature was also belatedly added to the Sports Complex bonds before they were sold.

Q. In the four categories, is there any question as to where among the four types of bonds the Port Authority consolidated bonds come down? [29] A. No question at all. They are revenue bonds. They have no state backup, moral obligation or anything of that sort. They are supported purely by the revenues from the projects which they have undertaken.

Q. Aren't they also supported by reserves? A. Well, the reserves, yes, of course. They are supported by the reserves but I guess the reason I said they were purely revenue, the reserves were all created from the revenues historically. That's where the reserves came from.

Q. Now, generally, Mr. Thompson, has there been an increase in the amount of municipal bonds sold over the years? A. Oh, yes, a very large increase. If we go back to 1948, the total sold was somewhere around two and a half billion including a little over a half a billion of revenue bonds. Last year the—there were 22,800,000,000 municipal bonds sold of which I believe 9,700,000,000 were revenue bonds or some 42-odd percent were revenue bonds. This, by the way, is not the total dimension of the tax exempt or municipal market because there is also the sale of notes in

large volume and actually last year 28 billion of tax exempt notes were sold. T 26-19 to 29-23.

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[30] Q. Could you discuss briefly, please, the ratings of municipal bonds? A. There are two recognized rating services, Moody's and Standard and Poor's. Each of them now rates the credit of an issue when a new issue is sold and charges a fee for so doing. There are four investment grade ratings which Moody states as Triple A, Double A, Single A, and BAA, and Standard and Poor's, the same down to the A., and then Triple B. These are all regarded as of investment quality and in none of those is it anticipated that default is likely to occur. The higher ratings are given [31] to qualities of credit where the margin of protection for future payment is larger and in the case of the Triple A, it is at some sort of a maximum.

There are ratings below those that I've stated. Most of them dealing with either bonds that are apt to be in default or that are considered highly speculative. I believe the BA and the Double B, they regard simply as highly speculative. Below that you begin to get toward default. T 30-15 to 31-9.

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[35] Q. What is the so-called "secondary market" in municipal bonds? A. The secondary market is a market in which present holders of bonds are able to resell their holdings and the secondary market has become very much larger in recent years because many investors are looking upon bond investments as a more active sort of a business, if a new issue comes into the market which seems especially attractive to them and they can sell one of their former holdings at what they think is a full or adequate price,

they will sell a former holding into the secondary market and buy the new issue.

Sometimes, the secondary market, of course, is used simply to obtain funds, if an institution or an individual wants to liquidate their holdings and use the money for another purpose. T35-4 to 35-19.

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[36] Q. How is the market structured in terms of buyers and sellers and intermediaries? A. The dealer firms consist of a commercial bank dealers department, dealers who specialize in municipals or who have the Municipal Department as a part of their overall security base and brokers.

There are, oh, a half a dozen or so brokers who act as intermediaries between dealers and they form a growing part of the market because some of those brokers have wires to all major dealers' offices and one way is if someone wants to sell a municipal holding, this is spoken of as getting somebody to put it on the penny wire and it goes to all dealers and in this way you are sure of getting the best bid because the offering is known to more people.

Q. In fact, are there a number of dealers in the municipal bond market? [37] A. There are a great many dealers. The dealer business centers, of course, in the New York financial community, but there are other centers in Chicago, San Francisco and some degree in Boston and there are dealers in almost all of the major and submajor cities in the country who do quite an active business in their local areas. [38] Q. Is the secondary market a competitive market? A. It is an exceedingly competitive market. As I indicated the Penny Wire helps to make it more competitive. No investor sells bonds these days without making sure that various firms have a chance to compete for the bonds.

Q. What is the pricing structure of that competition? A. Municipal bonds are generally sold on a yield basis, to yield a certain amount to maturity or to the first call date if that is the appropriate term to figure.

There are some that are priced on what is called a dollar bond basis, which really is not dollars but is a percentage of par. For example, if one of the outstanding bond issues were said to be priced at 85, it would mean that the buyer, if that were the bid for them, the buyer would be willing to pay $850 per thousand dollars of face value.

Q. And in fact when they quote and price yields are they calculated in fractions or in what manner? In other words, what are the differences in the calculation of yields when bonds are purchased on the secondary market—sold and purchased on the secondary market? A. Generally the market is stated in the basis points and segments of five basis points. That is, the bid will [39] be six twenty-five let's say, or six thirty-five for a certain issue to yield that much.

Q. What are those basis points? A. A basis point is one-one hundredths of one percent.

Q. Would an issuer of municipal bonds ever purchase bonds for its own account in the secondary market? A. Yes, especially if they had to [purchase] bonds outstanding [for] a required sinking fund; and many issues do, including most of the Port Authority issues.

And the sinking fund is set up in a way that requires the retirement of a fixed amount of bonds each year in order that by maturity the whole issue will be paid off. Now if the market is below the level and the interest rates are at a higher level than they were when the issue was sold, the issuer can go into the market and buy the bonds at a discount to its advantage. So this is always done.

Excerpts from Testimony of John F. Thompson

This is an advantage not only to the issuer; it is an advantage to the holder of the bonds because the sinking fund activity is a help to the market for his bonds. T36-9 to 39-19.

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[40] Q. In the municipal bond market what are the objectives of an investor? T 40-16 to 40-17.

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[41] A. The purpose of investors in investing in municipal bonds is to get the best yield they can relative to quality of the bonds. They are not simply buying something to be put away and the coupons clipped and the bonds to be paid at maturity.

They are looking to something that will cause a favorable relationship of yield to quality, maintaining its relative position in the marketplace. And this I think is the objective of most bond investors particularly the professional investment people and institutions. T 41-1 to 41-10.

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[42] Q. Would you explain perhaps with a little more detail the difference between a dealer and a broker in the secondary market in municipal bonds? A. Yes. A dealer in buying bonds either in a secondary or the primary market buys them for his own account and takes the risk that he will be able to sell them to an investor at a price which will afford him some profit and at least not involve him in a loss.

The broker, on the other hand, acts—works on a small commission and at no time do the bonds—are the bonds in the ownership of the broker. He doesn't have an inventory problem as most dealers have had particularly in the last year up until a month or so ago. It's been a serious one. T 42-5 to 42-17.

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Excerpts from Testimony of John F. Thompson

[43] Q. In your employment at Morton & Company and earlier at Scutter Stevens, have you had any dealings in the Port Authority bond secondary market? A. Yes. And several specific ones in my years at Scutter which I well remember.

On two different occasions through my recommendations [44] and advice and actually I think I made the contact with the dealers who then offered the bonds, over a million dollars each was purchased for the clients of Scutter, Stevens and Clark.

Q. And at the Morton & Company what would your involvement be in the secondary market? A. Well, my involvement in the secondary market is keeping in constant touch with the trading desk and the salesmen who are all involved in it as well as being asked from time to time for an opinion on the credit of something that's offered in the secondary market.

The credit judgment being a thing that is left to my responsibility in considerable part.

Q. Is it the practice at the Morton & Company to refer from time to time to credit rating reports prepared by independent credit rating agencies, and I show you P-1 and P-2 in reference to that question?

Would you identify P-1 and P-2, Mr. Thompson? A. Yes.

Q. And then answer the question if you can recall it. If not, I'll restate it. A. These are municipal credit reports prepared by Dunn & Bradstreet which then prepared reports independently of the later merger with Moody's. The question I—

Q. The question was, was it the practice and has [45] it been the practice—was it the practice at the time those reports were issued and has it been the practice at Morton & Company to refer to reports of that nature? A. Yes. It's

Excerpts from Testimony of John F. Thompson

always been the practice at Morton & Company to use the credit services of Dunn & Bradstreet and to refer to these in arriving at their judgments on the credits.

Q. And more specifically, how are they used? How are these papers, such as P1 and P-2 used? A. Well, they're used in providing information about the credit for those who are about to make the bid if it is a bidding situation; for salesmen, if they're discussing the credit with investor customers.

Q. Mr. Thompson, review, if you will, the situation with regard to the financial condition of commuter rail facilities in the Port district in the early 1960's as you understand it. T 43-20 to 45-17.

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[46] A. The situation in mass transit in those years was such that most facilities of this sort were operating at deficits. The Hudson & Manhattan Tubes which later became PATH were at that time bankrupt. There was a general recognition, I think, that the pressures on mass transit to keep fares down and the upward pressures on expenditures through union demands and threats of strikes were especially—were especially conducive to continued deficit operations and to lack of confidence in this type of operation as a vehicle for investment.

Q. What—

The Court: When you say there was a general recognition, by whom?

The Witness: In the investment community, your Honor. I guess I intended to imply that.

The Court: All right.

[47] Q. What [projections] were being made for the future of rail mass transit at that time.

Excerpts from Testimony of John F. Thompson

Mr. Sovern: By whom, your Honor?

Q. What projections that came to your attention were being made and would you then also answer Mr. Sovern's question, by whom? A. Certainly, the projection for the H and M, you didn't have a projection, you had a bankruptcy. I think then in the investment community that any project[ion] of what would happen in the mass transit was that it could only operate at a deficit.

Q. Do you recall any specific projections, in other words, can you point to anything specific or are you speaking from your general recollection? A. I am speaking from my general knowledge at that time.

Q. And you mention specifically the Hudson and Manhattan. In 1961, did it come to your attention that the Port Authority was proposed to take over the Hudson and Manhattan? A. Yes, this was a discussion and a proposal which was very much in the news in those days.

Q. What was your reaction to that? A. Well, my reaction to the Port Authority getting into that or other mass transit was one of concern be- [48] cause the Port Authority has always gone into projects which it could reasonably ascertain that they would become self-supporting, at least within a period of a few years of development and this seemed to be a different tact for the Port Authority to start on. T 46-3 to 48-5.

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Q. Did you look on the step as the final step of the Port Authority towards mass transit, the final step of the Port Authority towards mass transit? A. No, I think in common with the investment view of most things, anticipation is a key factor and if one step were made into mass transit, the question arose in the minds of most participants in the

Excerpts from Testimony of John F. Thompson

investment community, what comes next, what other projects in mass transit will next be undertaken, or projects.

Q. And did you have specific concern of the [49] Port Authority in your work at that time? A. Certainly in this respect, yes. A concern that the Port Authority might be pulled away from the revenue producing type of undertaking which it had up until then, into things that would get it into difficulty.

Q. Were you specifically involved in making recommendations towards clients of your firm with regard to Port Authority bonds at that time? A. I am sure I was, yes. I am sure I was.

Q. And what prospect did you see at that time for bonds of the Port Authority, both new issue and, if you will, the bonds that had already been sold by the Port Authority? T 48-16 to 49-13.

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[50] The Court: Do you have any specific recollection of some definite time period in 1961 when you might have considered what the prospects were for the Port Authority bonds?

The Witness: I do not think I recall a specific time period that far back, your Honor. I do recall that in 1961, this whole concern was being discussed and there were the beginnings of a discussion of what became the 1962 covenant as a device to uphold the credit of the Port Authority, but I do not think I can pinpoint it down as to the specific dates.

The Court: All right.

Q. What did you see at that time as the prospect for the sale of Port Authority bonds if the Hudson and Manhattan was taken over by the Port Authority? A. Well, it depended on what sort of overall restrictions were put on a situation in that respect. We all knew that the move to take over the Hudson and Manhattan was at least politically related to the construction of the World Trade Center and it could therefore turn out to be an isolated instance, but there was concern that it might not be, and I think this is what [51] eventually developed in the convenant.

Excerpts from Testimony of John F. Thompson

Q. If there had been no covenant, what would have been the effect upon the bond market?

Mr. Sovern: Objection, your Honor, if there had been no covenant, there conceivably would have been all sorts of terms and conditions which would have varied and the question as[ks] for an abstract and speculative answer.

Mr. Landis: The question as[ks] for the witness's opinion, it is hypothetical, but I think it is appropriate for an expert.

Mr. Sovern: The effect, I submit, has to do with the failure to specify, if you will, the hypothesis. As the witness testified, hundreds of conditions go into deals of this character. If there had been no covenant, we don't know what Mr. Tobin might have said about the absence of a covenant.

Mr. Landis: I think that is appropriate for cross-examination and Mr. Sovern will have the opportunity—

The Court: I would like to have all of the fact[s] or assumed facts in the hypothetical set forth in the record. In other words, are you asking him to assume that all of the conditions [52] of the consolidated bond resolution, the General Funding Statutes, the reserves required to remain in effect; are you also asking him to assume that the Port Authority would be continued to be managed by the same personnel

with whom he had experience in evaluating over the years, et cetera, et cetera, and are you asking him to assume also that legislation had been [con]currently pas[sed] by both States authorizing the takeover of the Hudson and Manhattan and the construction of the World Trade Center without any other conditions being imposed?

Mr. Sovern: May I add one condition, your Honor, to submit for your consideration, it is that the Executive Director of the Port Authority in whom he had such confidence at the time, he said the covenant was necessary. Had it not been enacted, it is entirely possible he would have taken a different view, so some specification of the question as to what Mr. Tobin was advising the community on this hypothesis seems to be called for.

The Court: I think you really ought to expand upon the question that you have asked in order to give it any meaning and also so that he **[53]** knows exactly what you are asking for the purpose of his cross-examination.

Mr. Landis: I will be glad to rephrase the question.

[54] Q. Mr. Thompson, if the Port Authority had been directed to take over the Hudson and Manhattan and build the World Trade Center without the covenant restriction of further involvement in rail mass transit, but assuming all other things have been constant and as they are, what would be the prospect for subsequent Port Authority bond offerings after that legislation?

Mr. Sovern: Actually, your Honor, on that hypothesis we know the answer. The stipulation reveals

the Commissioners would have refused to issue the section 7 certification, and that offering would have had to be renegotiated again on some other term.

Mr. Landis: Your Honor I submit we do not know the answer from the stipulation. I think there was speculation and representations made, but the question never reached the Commissioners. They never had to vote on the question. And it is not stipulated that they did vote on the question. And I would ask that the question be answered.

The Court: I am not certain that the stipulation actually would cover the answer which he hopes to elicit from the witness. Maybe he will get it and maybe he won't.

Do you understand the question?

[55] The Witness: I think so your Honor.

The Court: Then I will overrule the objection. You may answer the question.

A. All other things remaining equal and the authorization for the PATH takeover and the World Trade Center without the covenant would have resulted in my opinion in a less favorable market for the Port Authority bonds and a higher interest for the Port Authority bonds.

Q. Again if you will, although maybe it is repetitive, what was the reason for your opinion? A. The possibility of massive deficit operations getting into the Port structure.

Q. And what you referred to as a possibility, in fact was that concern borne out over the years since 1961 in terms of the deficits of rail mass transit? A. It certainly has been. I think it can be stated to be a proposition with tremendous foresight. The deficit of PATH was estimated at the time to be about five million dollars a year. As I understand it, it is running five times that.

Excerpts from Testimony of John F. Thompson

The operating deficit of the New York City Transit System during the current year will be $450 million to which must be added if we are to compare it in this context some $160 million of debt service on transit bonds, for a total deficit of $610 million. That is just the [56] Transit System in New York.

And I think this indicates that the fears of the investment community were well taken. In transit you are constantly—as the Port Authority recently found when they hoped to increase the PATH fare to cut the deficit of PATH down a little; great pressure was put on them by the two governors not to do it. There is a type of pressure that is ever present in this mass transit business that just does not exist in other activities.

Q. Of course Mr. Thompson we all know that the Port Authority did in fact take on the Hudson and Manhattan, and the Port Authority did covenant the issuance of bonds in the '60s after 1962, and the interest rates in fact did reflect great faith in the Port Authority credit. How did that all come about? A. It came about by the adoption of the covenant by the two states in which they convenanted and agreed with each other and with the holders of all affected bonds, subject only to bond holders' consent for any change—and this is in the statute—that no deficit producing mass transit facilities would be undertaken save for certain permitted purposes; and those permitted purposes are measured by a fraction of the General Reserve Fund which today has already been exceeded by the deficit of PATH; that is the general reserve fund is 170 odd million, the [57] covenant would permit $17 million deficits, including PATH, for new projects, and the PATH deficit is in excess of that. So that there is no room there.

I think it was the result of this covenant not to go further in this field that upheld the credit and borrowing power of

Excerpts from Testimony of John F. Thompson

the Port Authority over these years, and that was its purpose. It was not to give some bounty to the bond holders. It was to uphold the borrowing power of the Port Authority as an agency of the two States for the enterprises which the two States had assigned to it. T 50-3 to 57-10.

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The Court: . . .

Do you know if anyone knew the terms of the covenant, aside from yourself?

[58] The Witness: Yes sir. And as far as investors are concerned, certainly the investors that were advised by Scutter, Stevens and Clark; but I can't say whether they in their own minds were acting on the basis of from my knowledge of the covenant. I remember very well in information meeting at the time I think of the first bond issue to be sold after the adoption of the covenant when this was explained not only to the dealers and underwriters, but to investor representatives, because I was then with Scutter, Stevens & Clark and was invited to this information meeting; and the covenant was explained in very great detail as something that investors could rely on and should rely on.

It was explained to them as a legally enforceable contract between the two States and themselves if they became bondholders.

And certainly the institutional investor had every opportunity to know about this; every offering statement, every official statement of the Port Authority since that time in the offering of bonds has contained a very well expressed explanation of the covenant and what it meant to the bondholder.

Sure there might be an investor somewhere [59] who bought a bond without knowing what he was doing. When I was at Scutter, Stevens we used to find out quite a few of those, because later they became clients and wondered what they had done.

But so far as the informed part of the investment community, and given the institutional basis of a large part of the municipal market, a large part of it is informed.

As far as the informed part of the investment community certainly they knew about the covenant and relied on it and were importuned to rely on it.

Mr. Sovern: Your Honor, I ask that the last sentence be stricken as a legal conclusion and unresponsive to the question.

The Court: I don't think it was a legal conclusion.

Mr. Sovern: That they relied on it.

The Court: I think he is expressing it as a factual statement, not legal conclusion, based upon his personal knowledge of his dealings with people in the investment community that bought these bonds. I assume that was the basis of the statement.

The Witness: Yes.

[60] Q. The speech you referred to, Mr. Thompson, that [was] made by Mr. Tobin, did you, in fact, obtain a copy of that in writing? A. Yes. I found that there was a copy retained through the years of that speech. When I asked my former associates at Scutter, Stevens and Clark to look in their files for things that related to this, and I found a copy of the speech which I know had been in my hands because the Port Authority had not put a date on the speech as it was printed and I pencilled in the date. I recognized my own handwriting of the date on that copy

of the speech and that speech, by the way, was made to a combined group of the Municipal Forum of New York, the Municipal Bond Club of New York and Municipal Bond Club of New Jersey which includes probably a thousand professionals in this business. T 57-23 to 60-15

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[61] Q. At the time that you have been testifying with regard to the 1961, 1962 period you have testified as to the speech by Mr. Tobin which has been introduced as P-36 and described by you as the transcript of that speech, was there discussion by parties other than the Port Authority at that time of the covenant and its meaning and its need [62] and meaning. Let me amend that. A. Well, I certainly remember a great deal of discussion within the investment community of this and what it meant and of the necessity for it.

Q. Well, perhaps it would be best to refresh ourselves to the interchange in the investment community that took place on a formal and informal basis.

There are trade associations, as I recall your testimony? A. Yes. The trade associations, the Municipal Forum, the Municipal Bond club, but, of course, people in one business come together in many ways.

They lunch together, they're on the phone together in making trades. These things get discussed in the course of the trade. There's a constant flow of information back and forth that when I was at Scutter and was doing some of the buying, there were several dozen salesmen that would call me from time to time and these things would have been discussed back and forth with them. There's a constant flow of information between the street and the investment community.

Q. So that when you say that the covenant, its need and its meaning were discussed in the community, are those

Excerpts from Testimony of John F. Thompson

the kind of communicating—communications means that you were referring to?

[63] A. Yes, also the covenent, of course, was discussed in reports like this Dunn & Bradstreet report, a credit report on the—T 61-20 to 63-3

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Q. Describe it by number. A. P-1 and P-2.

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A. These discuss the covenant and what it meant to the credit of the Port Authority.

Q. And— A. Also on the informal discussion, I spoke of this information meeting at which Austin Tobin made the basic presentation. The meeting was not just a formal sit-down meeting. It ended with an informal reception where people moved back and forth and around discussing the subject of the day and I well remember some of those discussions at the time.

[64] Q. And when the Port Authority bonds were sold subsequent to the adoption of the covenant do I understand your testimony to be that the Port itself made written representations with regard to the covenant?

Mr. Sovern: Objection, your Honor. There's been no such testimony and the question is leading.

Q. Did they, I'll rephrase the question. A. Yes. I think I stated in each official statement there was such a representation, very definitely.

The Court: Unless you're referring to some other written communication.

Q. You're referring to the official statement? A. Yes.

Q. For the identification in the record, a sample of the official statement has been marked in evidence in this stipulation.

Excerpts from Testimony of John F. Thompson

Perhaps it would be best if you would explain at this point, the nature and purpose of an official statement and perhaps some of the synonomous terms that are often used to describe it. A. Well, an official statement is the document which an issuing body presents to the investment community to fully describe the issue which they are about to offer and in so doing it, if it's a good official statement they fully describe their financial condition, they fully [65] describe the—either describe or refer to the statutes under which they're operating. If there are resolutions or ordinances which are in fact bond indentures, those are usually put in in full text, they were in the Port Authority official statements, occasionally they are summarized in some official statements that are done less completely. There are financial tables, there are indications of what the money is to be used for, the whole story about the financing is put into the official statement.

Q. What's the purpose of the official statement? A. The official statement is to inform the investment community about the forthcoming issue.

Q. And specifically with reference to purchases of bonds? A. Yes, as dealers in an important bond offering, as dealers we obtain and sent to our major investor customers, copy of the official statement. I might say, your Honor, from time to time, I've tried to write up a summary, so that some of the customers wouldn't have to go through the whole thing.

Q. They're fairly lengthy? A. Yes, an official statement can be [a] 50, 75 page document at times. A full letter-size. T 63-7 to 65-23.

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[67] Q. Getting back to the time in 1962 at the time of the adoption of the covenant, did the acquisition of PATH

change your understanding of the Port Authority's role in the understanding of the two states. A. It certainly was an entry by the Port Authority at the instance of the two states in a field they had not been in before and not an especially happy one. T 67-18 to 67-24.

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[69] Q. Were you familiar in 1962 with the projects and facilities that the Port Authority had undertaken prior to that time? A. I was.

Q. And what was the common thread through all those projects and facilities? A. The common thread was that each of these facilities, at least given a time of beginning and getting into operation, would be self supporting and would be able to support the debt incurred to build the facilities.

Q. Did the PATH signify a change in that? A. Yes, because the PATH anticipated a deficit from the start. T 69-13 to 69-25.

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[70] Q. Did the Port Authority prior to 1962 have other deficit facilities? A. Yes, from time to time, but I think most of those deficit facilities were in due course related to other facilities. I'm thinking of—my recollection, your Honor, goes back to when there were separate Port Authority issues for each of the Hudson River Crossings and my recollection is there were one or two of those where the amount earned was pretty thin related to the debt [service] but through the flow of reserve money, they were [71] taken care of. I think when the Port Authority went into the airport business there were probably some beginning deficits in the airport business, but overall the airports have worked out to operate profitably.

Q. Do you know of any specific project that the Port Authority went into with the prospect that it would over a

period of years operate for a long time at a deficit? A. Only the PATH.

Q. Are you aware of any other bond holder protections bearing upon the question of whether the Port Authority could get at that time, or the current time, get involved in other deficit facilities? A. I'm aware of I believe it's called—of the Section 7 requirement and also of the 1.3 coverage requirement to be qualified in the case of the issuance of additional bonds.

Q. And are there also reserves maintained? A. Oh, yes, the reserves, the general reserve fund was established by Port Authority resolution many years ago and it is maintained at an amount equal to 10 percent of the outstanding debt which, of course, is a strong feature of Port Authority bonds. There is also a Port Authority policy to keep total reserves equal to two years of debt reserves, I believe.

Q. In your opinion, do those tests and reserves [72] render the 1962 covenant superfluous in terms of bond holder protection? A. No, indeed.

Q. And would you explain that? A. Well, the 1962 covenant and its requirements, require more specific determinations by the commissioners, by the staff and the commissioners, as to the earnings or prospects of deficits involved and they are—well, in the case of the Section 7 requirement, the commissioners can simply rule or state their opinion that the requirement would not harm the holders of the outstanding debt. In the case of the 1.3 times [test], they are permitted estimates of future earnings to some degree as well as [of] the historical earnings. This is a test which might be complied with on the initiation of a deficit rail facility, and later be found to have not avoided deficits by any means as given the propensity of these deficits to greatly increase.

Excerpts from Testimony of John F. Thompson

The determinations which must be made under the covenant, I believe, are much more susceptible to active testing, by those looking at the Port Authority from the outside, and [give] those in the investment community a much more secure feeling about the future profitability of the Port Authority.

[73] Q. Are there any experiences with specific regard to the Port Authority that you would refer to—that when you say experiences, on comparable things? A. Well, the PATH deficit has turned out to be many times—it was estimated at about five million in the years when PATH was taken over and as I understand it, it is some five times that now.

Q. And with regard to the specific structure of the Port Authority and its place in the political realm, are there concerns? A. Yes. The Port Authority is the agent of the two states. They are from time to time susceptible to pressure from the governors and the legislatures of the two states and as I indicated earlier on the mass transit field, it's a field wide open to such pressures and that was indicated when the fare—when there was an attempt to raise the fare on PATH that I believe was passed by the entire Board of Commissioners and then was vetoed by the governors.

Q. Do you recall the nature of that veto? In other words, how it was effected in practice? A. As I understood it, the governors have submitted to them the minutes of the Board of Commisioners and they can veto an item in the minutes. This is my understanding of it.

Q. And, in fact, though, wasn't an application [74] actually made for a fare increase? A. Oh, yes. The application was made and it was submitted—the federal government gets into this, too.

The ICC was involved and the application was made to them and, as I recall it—and the fare increase was, I

Excerpts from Testimony of John F. Thompson

believe, adopted by the Board of Commissioners itself before it was vetoed.

Q. In fact, doesn't the covenant by its very language permit the Port Authority to involve itself in other deficit rail mass transit operations? A. It does within limits, yes, by its language and I believe that at the time it was adopted the limit was small because 10 percent of the general reserve fund then was somewhere around $7 million—yes—$7 million and it was estimated that PATH would incur a deficit of $5 million a year so that there was a little margin for another operation.

The covenant, of course, also permits mass transit operations that can be self supporting including—including support from the outside as it were.

Q. In that respect, how does it differ from the Section 7 test that you referred to before? A. Well, it's more—it's much more precise. It's based on calculations which have to be made.

The Court: Is that in the statute?

The Witness: Well, it's in the statute that the [75] deficit that is expected to be incurred cannot exceed the general reserve fund.

The Court: Yes, that part of the statute, but the statement which you just made that the certification that the facility would have to be self supporting is more precise as against—I would assume measured against the Section 7 certification? Is that in the statute?

The Witness: I don't know what you mean by more precise. T 70-16 to 75-10.

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[77] The Court: Okay. Before in your testimony I thought you had made the statement that

the certification required to be made by the commission[ers] under the terms of the covenant with respect to a self supporting facility was more precise than the certification that would have to be made under Section 7.

The Witness: Yes, yes.

The Court: Now, would you please explain that by comparing the terms of the Section 7 certification, if that's what it really is, as against the certification of the terms of, let's call it, the A part of the covenant.

The Witness: The Section 7 certification "Requires that the authority certify [at] the time of issuance of bonds for a new facility for the next ten years or during the life of the bonds, whichever shall be longer, in the light of its estimated expenditures; that it will not materially impair the sound credit standing of the authority or the investment status of consolidated bonds or the ability of the authority to fulfill its commitments."

Now, the covenant, without taking on an additional deficit, mass transit facilities in the [78] 1962 statute, sets up certain amounts which the deficit can reach. That's what I meant by precise.

This [Section 7] is all in general qualitative terms, "Materially impair the sound credit standing or the investment status of consolidated bonds or the ability of the Authority to fulfill its commitments." "Materially impair", I submit, is a phrase subject to considerable variation and interpretation particularly when it might be involved in a field where the political pressures are such as they are in the mass transit field or are such certainly as the investment community believes them to be in the mass transit field.

The Court: Now, would you compare that with the covenant requirement of the certification.

The Witness: The covenant is that they must certify that the project will, one, be self-supporting—

The Court: I'm only concerned with that portion of it.

The Witness: Including the debt service or that it will have a deficit which, combined with the—

The Court: I'm not concerned with that part—what I call the B part of the covenant's authorization of mass— rail mass transit facilities. The only language which I take it that you derive your [79] opinion as to the quality of the certification is that which begins "The Port Authority must determine that the proposed additional passenger railroad facility is self supporting"? Am I correct in that?

The Witness: Yes, but, of course, those of us that are professionals in the field read the statutes also, your Honor.

The Court: Well, I'm quoting the statute. T 77-2 to 79-8.

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Mr. Landis: You're talking about the deficit [80] that is expected to be incurred—

The Court: No, no. I'm talking about the definition of self supporting facilities.

The Witness: Well—

The Court: He said that there was a more precise standard or certification that was required than with respect to the certification required under Section 7.

The Witness: May I answer that further, your Honor?

Excerpts from Testimony of John T. Thompson

The Court: Well, taking a look at this—

Mr. Landis: Here is the exact language. This paragraph is what your Honor refers to, I assume.

The Court: I can't—

Mr. Landis: "And other railroad facilities shall be deemed to be self supporting as of the time".

The Court: Right.

Mr. Landis: If you want, Mr. Thompson can read it aloud and then we'll know exactly what he's—

The Court: No. He can read it to himself.

Mr. Landis: All right.

The Witness: Now, self supporting, your Honor —although it sounds as though it can be a qualitative [81] phrase is not, at least not in our business.

Self supporting means that the revenues shall be estimated to be at least as much as the operating expenses plus the debt service which is a mathematical requirement that does not appear in Section 7, which only requires certification that it will not materially impair and that's what I meant by more precise. T 79-25 to 81-8.

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Q. Now, specifically, Mr. Thompson, do you know whether the 1962 covenant was looked to in the purchase of Port Authority bonds since 1962? A. Oh, yes, very definitely. T 81-13 to 81-16.

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Q. Would you explain its relative importance since 1962 in the minds of purchasers of bonds? A. Its importance in the minds of purchasers of the bonds [82] has been that it prevented the Port Authority from getting into a massive project producing deficits in the mass transit field or several such projects.

Excerpts from Testimony of John F. Thompson

Q. And did you personally look to the covenant and depend on it? A. Oh, certainly. That was—that certainly was an important and significant part of what I presumed we were buying for our clients when we purchased those bonds that I speak of.

Q. Which were those, just to make sure it's clarified? A. This is when I was at Scutter and there were at least two instances where we purchased Port Authority bonds for several clients. In each instance, the total amount was at least a million dollars of bonds.

Q. If the covenant had not been enacted, would those purchases have been made?

Mr. Sovern: Objection, your Honor, for the same reasons as before. The other elements in the hypothesis have to be specified for a question like that.

Q. Assuming everything else to be equal, but if the covenant had not been enacted would those purchases have been made? A. Assuming everything else to be—

[83] Mr. Sovern: I'm sorry, your Honor. The question has to be with the recommended purchase, not whether they were—

The Court: Right.

Your role then was strictly as an advisor?

The Witness: Yes, yes. It was—I advised the transaction and after consultation with the client sometimes completed the transactions and that's the reason for—

The Court: Well, would you have recommended, then, the purchase of the bonds?

The Witness: I would not have recommended them at the price [at] which they were then offered. T 81-23 to 83-13.

Excerpts from Testimony of John F. Thompson

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[84/85] Q. Was there some regard given to the pattern already established by the Port Authority in evaluating the strength of the covenants? T 84/85-7 to 84/85-9.

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A. Your Honor my own opinion and those I associate with in the various professional capacities all felt that this was a binding covenant not only because of the way it was stated and the way it was presented, but also because of [86] certain past contracts that the States had entered into with Port Authority bond holders.

Now in the 1931 legislation there was an agreement by the two States that no competitive crossing with the Port Authority crossings be built within a certain distance from those crossings. And that was always regarded as part of the contract with the bond holders.

And it was so highly honored by the state of New York that when they built the Throughway they built the Throughway bridge, the Tappan Zee Bridge over the widest part of the Hudson River in compliance with that contract, which they and the State of New Jersey had jointly made with holders of Port Authority bonds.

Q. If you knew that the covenant would later be repealed would you have recommended the Port Authority bonds during the '60s? A. No.

Q. Is there some relationship with regard to that feeling to the moral obligation bonds of the two States? A. Well there very definitely is in the investment community. There is a strong feeling about this. Let me give you two examples, if I may your Honor.

The repeal of the covenant was recommended by the Governor of New Jersey approximately one week after sale of the $300 million Sports Complex issue. That issue was

Excerpts from Testimony of John F. Thompson

[87] saleable at the time only because the Legislature had added the so-called moral obligation to its commitment.

In my opinion—and I have heard no professional investment person who disagreed with this; in my opinion if that recommendation by the Governor had been made one week before the sale of the Sports Complex bonds instead of one week after, the bonds would not have been saleable; because the investment community was saying about the repeal of the covenant, and has said about it: If a legal covenant can be repealed by the States, what confidence can we place in their moral obligation?

We have run onto this in an even broader field. My firm was the number two manager in a syndicate which last week underwrote $150 million and sold them of Power Authority bonds of the State of New York.

Now the Power Authority is not dependent upon a moral obligation. It is dependent on its own revenues which are from the sale of electric power. It is about as far removed from any emotional, or as far removed from the feeling I just stated as anything could be. And yet we found in several parts of the country that there were many institutional investor portfolio managers who had themselves adopted or their investment committees had adopted a rule that there be no further investment in anything in New York State or New Jersey due to the repeal of the covenant.

[88] Q. Mr. Thompson, are there any Port Authority bonds in Morton and Company's ownership at the present time? A. None.

Q. In fact isn't it customary for Morton and Company to carry an inventory of municipal bonds of certain municipal buyers? A. Yes, we generally carry some inventory.

Q. What is the policy now with regard to Port Authority bonds? A. We have not had Port Authority in the inventory since the repeal of the covenant.

Excerpts from Testimony of John F. Thompson

Q. Prior to commencement of this litigation did you as part of your duties as vice-president of Morton and Company have occasion to prepare any papers analyzing possible Port Authority involvement in community rail mass transit? A. Yes.

Q. I show you P-3 and P-4 and ask you to describe those in the context of that question? A. P-4 was as noted at the top still in draft form. Some of the people with relation to my firm, especially Mr. Morton himself, have been influential in public affairs over the years. And he asked me to prepare something along the lines feeling that discussion of repeal of the covenant was coming, to prepare something along the lines of what [89] might possibly be done within the boundaries set by the covenant; and to review also the procedure for getting bond holder consent for changes.

In this draft I did this. This draft was being used only for internal discussion. And at some point in it I made some suggestions about an overriding toll on the tunnels and bridges, which later on my lawyer friends advised me was not possible for one reason—and I was even then suggesting that the States do this and not the Port Authority—but they advised me that there was an inter-State commerce constitutional question here, and that probably what I had suggested was not feasible. T 84/85-22 to 89-12.

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Q. Mr. Thompson I believe you described one document. I believe you said, while it was a draft, it was never committed to any further form. [90] A. That is correct, it was never committed to further form. In early 1974 when this, actually after the Governor of New Jersey recommended repeal, and the recommendation of repeal by the Governor of New Jersey was a striking event to the investment community—I almost used the word shocking—for the reason

Excerpts from Testimony of John F. Thompson

that years ago when repeal was attempted, it was Governor Cahill of New Jersey who said: No, there is a contract there and we won't do it. So when this Governor of New Jersey recommended repeal it was a considerable shock to the investment community.

And I was asked to write up something in an attempt to be useful in persuading those in power that repeal should not be undertaken. And the memorandum described as P-3 is the memorandum which resulted from that effort.

> The Court: Well, the then Governor of New York was also advocating repeal and had recommended it several times, and indeed the New York Legislature had already passed a repeal.
>
> The Witness: In 1972.
>
> The Court: Yes.
>
> The Witness: That is what I mean when I say Governor Cahill was the one who stopped it two years ago.
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> The Court: Was the investment community equally shocked when the then Governor of New York advocated a repeal and the New York Legislature [91] actually voted a repeal?
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> The Witness: I think to say equal shock would be unfair your Honor. Let me see if I can explain it. When Rockefeller signed the repeal in 1972 he issued a statement which in its terms was very conciliatory. It had words in it like: I shall be conferring with the Governor of New Jersey to try to work out something here that will not impair the credit of the Port Authority. It was a less final thing.
>
> I agree, it was after that that Governor Cahill definitely decided he would not go along. I won't say there was not shock in the investment community; there was. And the reason I mentioned this

later event is that once the Governor of New Jersey was, from the investment community's point of view the one who stopped it, then to have a new Governor of New Jersey say I recommend it, this is the event I referred to as somewhat of a shock to the investment community.

Q. Mr. Thompson you have indicated shock in February of 1974. But isn't it true in his campaign in 1973 Mr. Byrne at that time mentioned the fact that he intended to repeal the covenant? A. It very likely is. I don't recall—not being a [92] resident of New Jersey I did not follow the campaign as closely as some. It is one thing to make statements in a campaign, if I may say so, and another to come out with a formal recommendation, because there often is leeway.

The Court: Maybe that is why you were shocked because the politicians kept [this promise].

The Witness: I had not thought of it that way your Honor.

Q. What in your opinion has been the effect on the Port Authority's secondary market as a result of the repeal? When I say the Port Authority's secondary market I refer of course to the secondary market in Port Authority bonds. I am using a shorthand term. A. Yes, to be sure. And there had not been a primary market since then because they had not sold a bond issue. The market has been adversely affected by the repeal. It is not possible to measure the adverse effect simply by comparing market prices I believe.

There was a time before the repeal when Port Authority bonds traded in the market very much as some of the other

Authorities, major Authorities of State bonds do. And if a bank or insurance company with a five million dollar holding of those bonds came to a dealer and said: I want to sell these; what will you bid? He could get a bid that would be pretty much in line with the quoted market.

[93] What we have now is a market that is unusually thin because present holders are not willing to sell. Most of them have been advised by their portfolio managers or their professional advisors to hold on and see what develops here. Most of them believe that the covenant is protected by the Impairment Clause of the Constitution.

Mr. Sovern: I move that that sentence be stricken. He does not know what most of them believe.

The Court: No; I think you really ought to qualify it.

A. I will qualify it and say all of the professional investors I know and have talked to believe that the covenant is protected by the Impairment Clause of the Constitution. Consequently they do not want to sell at a sacrifice. This I believe was the position taken by United States Trust Company after they [launched] this lawsuit.

I have been asked by a number of our customers what my advice is at this time. And I have given the same advice, to hold on.

As a consequence the flow of bonds into the market is much much less than it normally would be.

You could get a flow into the market by one of two things. One would be a brand new issue coming into the market. The other would be some investor who decided not [94] to go along with this type of advice, but to sell his five or ten million dollar holdings. In my opinion in

either one of those events the bid for the bonds would be substantially below the market as it is quoted today.

Some of us have discussed the possibility of an interest rate on a new issue if one were to be sold, an—

Mr. Sovern: Your Honor I am going to object to this.

The Court: I will sustain the objection. T 89-23 to 94-9.

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[100] The Court: All he wants to do is get the witness to say it would cost the Port Authority more money today in interest to sell a bond with a repeal than it would without the repeal.

Mr. Sovern: He has testified to it twice.

The Court: I agree it might be repetitious, but that is all he wants to get him to say.

Is that your opinion?

The Witness: Yes, it would cost considerably more because of the repeal.

The Court: No matter what the purpose of the bond issue was?

The Witness: At this point, I would say—

The Court: How much of this is an emotional reaction to the shock which was experienced by the repeal and how much of it was based upon a sound intellectual analysis of the financial position of the Authority?

The Witness: I think the latter, your Honor, [101] but the sound intellectual analysis also has to include the fact of repeal and the fact that this litigation is not resolved and therefore if the Port were to come to the investment community with a new issue, they would have to present it and expect

to get a bid, assuming that the worst happens from the investment point of view.

Q. Will you explain the worst? A. The worst meaning the United States Trust Company does not win this suit.

Q. Going back, Mr. Thompson, to the point of time at which there was a very serious and active discussion of the repeal, a point of time which you identified as starting in February of 1974, have you kept track of the commentary in the investment community and the press with regard to that activity? A. Yes, in some detail.

Q. And in fact, did you involve yourself in your posture as a trade association representative in the process, the legislative process at that time . . . . T 100-6 to 101-20.

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[103] A. Yes. [As shown in] P-5, I was one of a group that conferred with Dr. Norman Hurd, who was a secretary or executive assistant to Governor Malcolm Wilson. I was there as President of the Municipal Forum of New York. Mr. Weeden, as representing the Municipal Bond Committee of the S.I.A. Mr. Pratt was there representing the New York Clearing House Banks; Mr. Beason representing the Dealer Bank Association and Mr. Putman was there as the representative of the New York Area Organization of the Securities Industry Association.

This letter was written after our conference, and as it states, after a conference of that sort, your Honor, you think of several things you wish you said. This letter was to do that.

The second letter to Chairman Ronan [P-14] was the third in a series. I had written a letter to the New York Times which was published, I believe, in early May, urging

that the covenant not be repealed and urging the disadvantages to everyone and everything concerned, including any help the Port might give mass transit.

The letter was answered by Chairman Ronan and P-14 is my response to him. His response was also published in the Times. At that point, I determined I should respond to him but that the public discussion had [104] gone on long enough and I simply wrote this letter to further state the case to him personally. T 103-2 to 104-2.

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[115] Q. Have you had occasion since the repeal of the covenant to also discuss the matter with investors as distinguished from other members of the investment community? A. Yes, yes. I've discussed it with some of our customers at the request of the salesmen who ordinarily cover them, as the expression goes in the trade.

Q. And have you given them advice in response to requests? A. Some of them have asked what do you think, what—should we hold on to the Port bonds we own? Should we buy more at this time? I've given them the advice that I would hold on for the reasons that I stated earlier and I will repeat now—

Q. It's not necessary unless the Judge—

The Court: No, no. He testified as to that.

Q. —requests it. We have it on the record.

And with regard to—you said you also gave them advice with regard to the—A. With regard—

Q. —with regard to the purchase? A. With regard to purchase I simply for the most part agreed with them that it wasn't a very wise thing to in effect buy into a lawsuit.

[116] Q. And did you recommend to your firm a position as regards the inventory of the bonds? A. Yes. I

recommended and I found the rest of the firm in complete agreement that we should not put Port bonds in inventory at this point because of having to be at risk in whatever we carry in inventory.

Q. In that regard, how would you characterize the Port Authority secondary bond market at the present time? A. Well, as I said earlier, the Port Authority secondary market is very thin at the present time and the supply of bonds coming into the market is much smaller than it has been in the past or than it is for other authorities in the state system. T 115-2 to 116-13.

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Q. Do you have an opinion as to the effect of the United States Trust Company lawsuit that is being heard here today on the secondary market for Port Authority bonds? A. Yes, I think the lawsuit filed immediately by the U.S. Trust Company had a very sustaining effect on the market in that it indicated to bondholders that their interests [117] were being actively protected and seen to and that if it hadn't been for that, the market probably would have been —would have been worse and it would have moved lower than it has. I think that's had a sustaining effect.

Q. Now, with regard to the specific comparison of Port Authority bonds to other bonds of other agencies, municipal agencies, during the period in question, I would like to show you a series of exhibits which—I'm sorry—not a series but two exhibits.

Specifically P-89 and P-90. These are the ones that you know as the—T 116-20 to 117-11.

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Q. Two bonds are reflected there, are they not? For the record, would you indicate those bonds? A. The bonds are the Port Authority of New York and [118] New Jersey, 6

percent bonds of February 1, 2006, and the Massachusetts Port Authority, 6 percent bonds due July 1, 2011. The bonds are comparable as to coupon rate and both are long maturity so they are comparable [as] to maturity.

Q. Mr. Thompson, going back for a moment, before going on with this specific chart, you previously testified as to what a dollar bond was. Is it true that these are both dollar bonds? A. Yes. These are both traded in the market on a dollar basis which means a percentage of par value.

Q. Is that what's shown in the left-hand—A. That's what's shown on the left-hand margin.

For example, when this hits, when one of these lines hits 85, it means that the market would pay $850 for $1,000 par value of bonds.

Q. And in the market what does the bid price mean? A. The bid price is the price offered by a buyer or a prospective buyer. It—sometimes a bid and asked quotations are obtained which doesn't necessary fully reflect the impact of the market but I gather that this is an accurate portrayal of the bid side of the market for these two issues.

Q. I show you an exhibit which has been marked P-93. Do you understand that to be the source of the bid prices?

[119] A. Yes. This is my understanding that the prices for the Port Authority 6's were from Weeden & Company and the Massachusetts Port Authority are the prices from Clifford Drake.

Q. Are those reliable sources? A. Yes.

Q. Now, would you, before going on to the specific question that we touched on before, the comparability of these two issues, would you describe the Massachusetts Port Authority as you know it? A. Well, the Massachusetts Port Authority like the Port Authority here, operates the airport. They also—they don't have the numerous toll

facilities that this Port Authority has, but they do have one of the leading ones in it—what used to be the Mystic Bridge so that their business is in the same sort of revenue producing projects that the Port of New York Authority—Port Authority of New York and New Jersey is in.

[120] Q. What geographical area are they in? A. The Boston metropolitan area.

Q. And now with specific reference to the two issues shown on P-89 and the bid prices which are listed on P-90, what other similar and if any, dissimilar characteristics of the two issues are there? T 117-23 to 120-7.

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Q. The two issues that are specifically listed. One I say "issues," two bond issues? A. The two issues have the same credit rating by their rating agencies, and as I said earlier, they are similar in other respects.

Q. In the marketplace, would the 006 and 011 maturities be considered similar? A. Yes, because when 006 is out over 30 years and when you get beyond 30 years' maturity, the change in price for a change in yield, does not vary very much from there on out. So they would both sell as long-term issues and be quite comparable.

Q. Could you describe the intrinsic security behind the two issues? A. Well, the intrinsic security is the revenues [121] of the projects managed and other aspects of financial security, both of which are involved in the A rating.

Q. Do you find that these two issues are comparable in all characteristics that you feel are important? A. Yes.

Q. And how about the external factors other than the characteristics to which you have testified, market factors and the like, are they comparable or are they subject to the same internal factors in that regard? A. Well, they are each subject to external factors reflected in their own

Excerpts from Testimony of John F. Thompson

states, in their own locale, so they might either track together or vary as they have here.

Q. Would you characterize the relationship as demonstrated here between the bid prices of the two issues from July of 1973 to April of 1974? A. Yes, during that period, the two issues, in price, practically tracked each other. The line crossed on occasion. T 120-10 to 121-22.

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[127] Q. How would you characterize the relationship from April, '74, to December, '74? A. There was a growing spread betwen the two bonds which was unusual compared to their past history as shown.

Q. What factors changed at or during the period in question? A. The fact that changed was the repeal of the 1962 covenant by the two Legislatures and signed by the Governor.

Q. Were there any other changed facts that you know of? A. Not that I know of, no.

Q. Do you have an opinion as to the impact of that fact on the prices as demonstrated on the chart? [128] A. Yes, in my opinion, the spreading out of the two markets was due to the repeal of the covenant.

The Court: Wouldn't it also be due to the opinions expressed by persons such as yourself and their recommendations not to purchase Port Authority bonds?

The Witness: I think our recommendations not to sell are much more important, your Honor, because there were no new issues coming into the market so that a purchase recommendation was not as appropriate as it would be if they were a new issue. The recommendation to hold on, I think, had much more impact on the market.

Excerpts from Testimony of John F. Thompson

Q. What was that impact? A. To sustain the market.

Q. For which? A. For the bonds of the Port Authority of New York and New Jersey.

Q. In other words, the red line as shown on the chart would deepen even lower? A. If the market were confronted with large volume sales of bonds of the Port Authority of New York and New Jersey, in my opinion, the Port bonds would dip considerably further. T 127-10 to 128-25.

[130] Q. What does the chart show from the pattern from July, '73, to April, '74, P-91, I am referring to, for the record? A. It shows the same pattern as the other, that they track through that period.

Q. And what does P-91 show from April, 1974, through December, 1974? A. It shows the same spreading out, showing that the Port Authority of New York and New Jersey bonds suffered more in the market during that period.

Q. What conclusion does P-91 and, of course, P-89 tend to support? A. It supports a conclusion that even with a limited market in supply which has not fully reflected the bad effects of the repeal because of lack of volume, but even the limited market shows that the Port Authority bonds had been adversely affected by the repeal. T 130-1 to 130-18.

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Cross-Examination by Mr. Sovern:

[131] Q. Mr. Thompson, you testified, I believe, that you know of no other reason for the Port to behave as the chart reflects other than the passage of repeal by the two Legislatures and the signatures by the Governors. Is that correct? A. Yes, sir. T 131-19 to 131-25.

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Excerpts from Testimony of John F. Thompson

[132] Q. If you know of any other facts, would you state them now, please, Mr. Thompson. A. No, I don't know of any other facts or causes.

Q. Thank you. If you look at Plaintiff's exhibit 92, you'll see that the—T 132-13 to 132-17.

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Q. —from July 19 to August 23, the price was—the spread was four to five and a half points—

The Court: You're talking about 1974?
Mr. Sovern: Yes.
The Court: July 19 to—
Mr. Sovern: August 23.

[133] Q. Throughout that period the prices were relatively constant, varying 5, 5½, 5, 5½, 5½. I believe it's accurate to say it was only either 5 or 5½.

Why did it go to 8 on August 30 and still spread further in the weeks immediately following? A. I don't think one can pinpoint that sort of thing, sir. The best answer I can give would be that it was a gradual cumulative effect of recognition of what had happened.

Q. In other words, there was no recognition between July 19 and August 23— A. I didn't say there was no recognition. I said a gradually cumulative effect.

Q. Are you familiar with the story in the *Wall Street Journal* dated August 15, 1974, headed "World Trade Center Is Far Behind Plans For Filling Offices"? A. I probably have seen it, yes. T 132-20 to 133-17.

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[134] Mr. Sovern: We are marking as State's exhibit 1—well, I better give you this copy—we're marking as State's exhibit 1 the *Wall Street Journal*

Excerpts from Testimony of John T. Thompson

story dated August 15, 1974, which says, "World Trade Center Is Far Behind Plans for Filling Offices." Plaintiffs have a copy of this it [135] was produced from their files, your Honor.

The Court: Is there any objection?

Mr. Landis: Your Honor, I assume that this is done with the exact same stipulation that was placed on the newspaper articles that were offered by the Plaintiff in this case; that is, not to be considered as proof of the facts indicated in the article.

Mr. Sovern: I entirely agree with that. We're cross-examining about causes of price decline.

The Court: All right.

S-1 into evidence. T 134-20 to 135-12.

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[136] The Court: In any event, looking at S-1, do you recall having seen that article either in part or in its entirety?

The Witness: Yes, I think I saw it at the time, your Honor.

[137] Q. Well, would it have affected the price of the Port bonds? A. I would doubt it very much. The development of the World Trade Center has been a very gradual sort of thing. The investment community has been aware of slowdowns from time to time, of increases in the capital cost. And I don't think that the article covers anything striking enough to have any impact on the market. Certainly I heard no discussion of it in that respect at the time.

Q. You don't think it would distress bondholders to know that 40 percent of the space is unleased?

Excerpts from Testimony of John F. Thompson

Mr. Landis: I object to that. Again we are getting—

The Court: He is not offering it for the truth of that statement; but would a bondholder be affected if he saw such a statement in a publication such as the *Wall Street Journal*?

Mr. Landis: The way you ask the question is fine. That is what is assumed in the question, because we are operating on the stipulation that the facts that are stated in the article are not necessarily true.

[138] A. With that stipulation, your Honor, may I also answer that the sentence does not say that it is 40 percent unleased. It says about 22 percent of the entire complex. 40 percent of the commercial space is still unleased.

Q. That's correct. A. The rest of it is being paid for in rentals just as well as the commercial space.

Q. Would that trouble the bondholders?

The Court: In his opinion.

Q. In your opinion. A. In my opinion, it would not, because I suspect that there is close to 22 percent of the space that is not fully completed yet. I think the renting and the completion of the space is fairly well parallel. I think most institutional investors have gotten to the point where a news article alone does not frighten them.

Q. Do you know the present investment of the Port Authority in the World Trade Center? A. I know in a general way that it is around 750 million dollars or thereabouts.

Q. If I told you later figures showed it to be 800 million, I take it you would not find fault with this? [139] A. No, I won't quarrel with that. T 136-5 to 139-1.

Excerpts from Testimony of John F. Thompson

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Q. You recall the original estimate of the cost of the World Trade Center? A. I believe the original estimate was around 350 million dollars.

Q. If I told you it was 250 million dollars would you find that— A. No. I have seen that figure in some of the things that I have been reading if I am just not sure that wasn't the figure before it actually got started, that is preliminary figure, that one perhaps shouldn't fairly go back to.

Q. For the time being, let's take this: 350 million dollars originally projected, not preliminary, currently at 800 million, and the story says it is 22 percent unleased, bondholders unconcerned? A. I have already commented on the story. The rise in costs, I'm sure that some of the renting of the space must be tied to the rise in costs. That is generally the case.

Q. You have no other explanation for the increased drop in Port's at the end of August? A. No other explanation than the repeal of the [140] covenant, no.

Q. That's correct. Take a look at P-92 again, and you will see that in mid-October, 1974, the spread [closed] again, apparently.

The Court: P-92?

Mr. Sovern: Mid-October, 1974, P-92, the same chart we were just looking at.

The Court: Mid-October, that's right.

Q. The spread closed to 4. How would you account for that, Mr. Thompson, if the increase in the spread in August was the product of the delayed reaction of the repeal, why did the spread contract in October? A. I don't think one can pinpoint from week to week or month to month moves

in markets and exhibit them to any particular cause; over a long sweep, one can.

Q. You did attribute it to a cause. A. Over a longer sweep I did attribute it to a cause, yes, sir.

Q. You cannot account for the fact that the spread closed to 4 in mid-October? A. No. There are very often temporary influences that come into markets that have very little to do with developments; that have to do with somebody [141] for some particular reason being in the market or withdrawing a sale or something of the sort. It is not necessarily the result of developments. Markets do not work like computers.

Q. How temporary do you have in mind, daily, weekly, monthly or annually? A. Certainly a period of time such as represented by the widening of the spread here indicates something but—

Q. The spread closed to 4 on P-92, on October 18. And you know—that means it could conceivably have closed to 4 on October 12. This is the first date it is dated for, October 25. It was 4½ on November 1. That is a minimum period of three weeks at which it had closed to 4. Can you explain that? A. I have no particular explanation for, as I say, relatively short-term movements in the market. I don't think one can tie to those.

Q. You will notice the spread opened again in November 15, it is at 11. Can you explain that? A. No, I would not attempt, as I say, to explain these shorter term movements.

Q. That is still attributable to the repeal in June—Governor Wilson's signature in [142] June, Governor Byrne's signature on April 30 and the legislative actions on those signatures are still having their effect on the widening spread in November after contraction in October and having earlier had these other movements—that is your testimony? A. I think that is true as nearly as we can ascertain it, yes.

Q. What is the most significant factor working in the municipal bond market at this time and over the last year?

The Court: The most significant factor affecting prices?

Mr. Sovern: Yes.

Mr. Landis: Is this generally?

Mr. Sovern: Yes, generally.

A. At the present time the most significant factor is the reverse of what it was up until December or thereabouts in 1974.

Q. The bond market was generally depressed? A. Yes. T 139-4 to 142-20.

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[143] Q. I take it the municipal market like other bond markets were significantly depressed like all other markets in 1974. A. Yes. That is the reason the lines go downward. If the municipal bond market had been relatively firm the change in Port Authority prices would have been much easier to show than it is.

Q. The main determinate of the trend is a downward trend that was affecting all issues of this character, meaning municipal bonds. A. I suppose we could put it into figures here saying that the movement in the black line down to somewhere between 75 to 80 represented that, and the rest of the move of the red lines represented the Port Authority repeal.

Q. That is what I am trying to find out. That is your testimony. Would you come back to my question? You will recall it was your testimony that you could not account

for the increase in the spread to 11 on November 15. Do I accurately [144] state your testimony? A. Yes. I stated that.

Q. Have you seen the New York Times article dated November 10, 1974, and headed: Port Authority has fallen on hard times? A. Yes, I saw the article.

Q. Could that have had an effect on the price in November? Would you like to examine it? A. Yes.

The Court: I think it ought to be offered.

Mr. Sovern: This is marked as S-2 and offered in evidence.

The Court: Is there any objection?

Mr. Landis: Does the exact same limitation apply, your Honor.

The Court: To all of them, any newspaper article.

Mr. Landis: Not considered proof of the facts stated?

The Court: Not considered proof of the facts; unless there is a contrary statement at the time of offering.

Mr. Landis: Thank you, your Honor.

[145] The Court: I assume there are going to be some prices offered, quotations and the like.

Mr. Landis: We have already offered some.

The Court: These are abstracts.

Q. Do you recognize that article, Mr. Thompson? A. Yes, I remember that. T 143-6 to 145-9.

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[146] Q. Could it have affected the price? The price of New York Port Authority bonds? A. It is possible to some degree, but again I don't think there are many holders of Port Authority or other large agency bonds or

prospective buyers who depend on the news media for their information. Also I notice that this article includes among other things a discussion of the repeal of the covenant; so that again it was raising that question.

Q. Do you think that perhaps some bondholders, irrespective of whether they take their advice from the daily news—I apologize; that was [147] inadvertent, the *New York Times*, may fear that the price of their security will be affected by everyone else reading about it in the *New York Times*?

Is that news in the newspaper a fact or factor that an investment advisor takes into account in deciding whether to buy, hold or sell? A. I would say probably only to the extent that he finds that it is proved in the lower market price and he knows better than to have—

Q. Would you say that this was proved in the lower market price? A. I just wouldn't say, because I have never related these two things specifically.

Q. Isn't this article a little strong for financial reporting, Mr. Thompson? I call your attention to the assertion that the Port Authority is at something of a low point in its long career. As one Commissioner of the Authority said, it is dead in the water. T 146-14 to 147-19.

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[149] Q. . . . Perhaps I should read several, then if you can tell me whether you share my sense that those are strong words to describe a sense of security.

The third paragraph, "Deterioration of the huge agency attributed this statement to officials and commissioners of the Port Authority, the deterioration of the huge agency may be more serious than anyone had previously imagined. The principal problem facing the agency is its inability to sell bonds or borrow money."

Excerpts from Testimony of John F. Thompson

Would you say those statements bothered a bondholder? A. Well, can we go on after that?

[150] Q. Anything you would like to read. A. "A bondholder's suit has scared off potential lenders and underwriters."

This is one of those types of newspaper reporting where the reporter stands on his intellectual head. This is nonsense. Bondholder's suit did not scare off potential lenders. The repeal of the covenant scared them off and just because Frank Prial does not know that and does not write in the *New York Times,* does not matter a darn to investors.

Q. Mr. Thompson, we don't hold you to the knowledge of the fine points of evidence.

The story is not being used to establish that these statements are true, but that Frank Prial of the *Times* made them and presumably a million people read them, some of them Port Authority bondholders.

Now, you added a sentence to a number of others I read and there are more to come.

Would they frighten a bondholder? A. I would not think that any professional investor in Port Authority bonds, and the Port Authority bonds are widely held in institution and investment accounts, I would not think any [151] professional investment manager would be influenced or get his facts from a newspaper article, and, as a matter of fact, I would think that most of them would get about as far as the passage which I just read back to you, and then say, "Well, this guy doesn't know what he is talking about anyway, forget it."

Q. Did you read this story through to the end when you saw it in the *New York Times*? A. I probably did because I am professionally concerned with all those sort of thing, but I did not read it with any feeling that I was being informed.

Excerpts from Testimony of John F. Thompson

Q. Why did you keep all those clippings to which I objected before in your file? A. Most of them dealt with events. This is what the newspapers call "analytical" reporting or news analysis or something like that. Sometimes they mark it as that.

Q. Let's go on.

In the next paragraph, following the one from which you read, "Some of the impressive facilities of the Port Authority have stopped making money or in some cases never started."

That sounds like the description of an event or series of events to me.

[152] Would that concern bondholders? A. If bondholders obtained information to that effect from reliable sources, from reports by the Port Authority or from the credit agencies or someone to whom they look for reliable information, it might affect them, but I am not at all sure they would be bothered by a newspaper reporter saying it.

Q. You are not at all sure they would be bothered, but it is possible? A. Well, it is barely possible that the most uninformed might be.

Q. The next paragraph says that it is assumed—

> The Court: Before we go further along this line, what percentage of the Port Authority bonds of series such as that which is reported on P-92, the 2008, what percentage would be held by individual investors, let's say, up to the $50,000 category as against the institutional investor?
>
> The Witness: Your Honor, anything I said in response to that would really be a guess.
>
> The Court: I realize that, but based [153] on your experience and knowledge in the underwriting of these issues.

The Witness: I think a larger proportion would be in institutional hands, and I might say that many individuals who would own these Port Authority bonds or own other tax-exempt bonds, really have their accounts professionally managed by bank trust companies or by investment counselling or investment advisors of other types, so that I would think a very large proportion, one way or the other, would be under professional guidance.

The Court: With such a thin market for these bonds as you have described it after the repeal of the covenant, wouldn't the offer of a relatively small quantity of bonds have a greater effect upon the price than would otherwise be the case?

The Witness: I suspect that is true, yes.

The Court: In other words, an article such as this if published, would not have to reach necessarily the institutional investors and have them act upon it, but if a number [154] of individual investors had read it and decided that they should sell, that could have a pronounced effect, given the condition of the market as you have described it?

The Witness: Most of those individual investors who were even without professional investment advice in the sense that they paid a fee for it or something of this sort, most of them, I think would talk to their own dealers from whom they bought the bonds before they arrived at a decision like that. They would have to say, "What do you think of this article, what do you suggest doing?"

I spend a great deal of time calming down fires from articles on a number of things, not necessarily the Port Authority, but somebody asked one of our

salesman, "What about this article on UDC," or something of that sort, and then I have to read it and give them some interpretation of it in terms of what I can find out about the actual situation.

Q. You say you spend a fair amount of time calming down fires when there are adverse press reports.

Are you always successful? [155] A. Generally.

Q. In your opinion, do some investment advisors not choose to put out those fires? A. I don't know that I can answer for all investment advisors. None that I know of would fail to act responsibly.

Q. You would not expect, though, that all investment advisors would be one hundred percent in allaying bondholders concerns in the wake of a newspaper story that was highly damaging in the terms used, would you? A. I don't think I'd have any way of judging that, sir. T 149-12 to 155-13.

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[158] Q. I am asking you whether in your opinion bondholders would be concerned to read a *New York Times* story calling a Port Authority official, to be sure unidentified, as saying the World Trade Center is a white elephant? A. Of course, I can't answer that an absolute no. I have no idea what all bondholders might—any and every bondholder might think. Any bondholder that I know of or have had contact with, would, if he were concerned about that, call up somebody that he thought knew and ask him about it and that's about the size of it.

Q. What would he find out if he called up and asked somebody whether he thought the World Trade Center was a white elephant? A. Well, I was really pushing back to a place where some figures are given there. I don't think

Excerpts from Testimony of John F. Thompson

anybody buys and sells on phrases like "white elephant." [159] I hope not. T 158-8 to 159-1.

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[160] Q. So your opinion is that this *New York Times* story of November 10, 1974, had no discernible impact on the Port Authority bond prices? A. It had none that I could identify or know about.

[161] Mr. Sovern: I'm sorry.

The Court: Are you saying the article as a whole?

Mr. Sovern: The article as a whole and in its various allegations.

The Court: Because I thought you had testified before that with reference to the article as a whole that it could possibly [have] affected the price to some degree but you weren't prepared to say how much.

Mr. Landis: Well, that wasn't the question that he asked. He asked, would you testify that it has no discernible impact and he said no, none that I can identify, and I think before he just allowed that the possibility existed.

The Court: All right.

The Witness: I believe that is the difference in the two answers. I hope they're not inconsistent.

The Court: No, they may not be.

Mr. Sovern: I'm sorry. I'm absolutely confused.

By Mr. Sovern:

Q. I understood your testimony to be that this article had no discernible impact on the price of the Port Authority bonds—[162] A. So far as I can indentify.

Q. And you cannot account for the growth in the spread of price between Port Authority bonds and Mass Ports to

Excerpts from Testimony of John F. Thompson

11 on November 15? A. Not in any particluar—not by any particular event, no.

Q. And that's because the short term swings are not instructive—how long a trend line do you need before you can effectively identify a cause of a growth in price spread? A. I don't know that I can state a fixed rule on that but—

Q. Give me a range; year, three months? A. When it gets to six or eight months as this appears to be, then I think you have a trend. T 160-22 to 162-15.

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[163] Q. Let's take May 10. What was the spread on May 10, 1974? T 163-8 to 163-9.

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A. Shows five points.

Q. Now, May 10, I take it, you understand followed the passage of the New Jersey legislation and signature by Governor Byrne and the passage of the New York legislation but not yet the signature by Governor Wilson, correct? A. Yes, I believe that's correct.

Q. So the five point spread, I take it, [164] Governor Wilson's signature should have an effect on the spread that would aggrevate it over the long term? A. Well, markets are just not that automatic, sir. T 163-18 to 164-3.

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[165] Q. On May 10, the spread between the bonds was five points. On May 10, Governor Byrne had signed the legislation—had already signed the legislation passed in New Jersey's legislature and both Houses in New York had passed the repeal and Governor Wilson had not yet signed it.

On your analysis and in your opinion I would anticipate that the signature by Governor Wilson would aggravate

the spread. Am I correct in this? A. If market[s] acted automatically on events, yes, but markets act on anticipation a great deal of time.

Q. So, in other words, Governor Wilson's signature might not have adversely affected the spread? A. If it were already anticipated, it might not.

Q. Governor Wilson, then, would reduce the spread? A. Definitely not.

Q. No. Do you know what the spread is today, seven months after Governor Wilson's signature between the two bonds referred to in P-92?

The Court: You mean today?

Mr. Sovern. Today—yesterday, actually, your Honor; today's *Times.*

A. Well, newspaper quotations?

Q. Yes. [166] A. I wouldn't take that as an accurate reflection of markets.

The Court: Well, do you happen to know yourself—

The Witness: No, I don't know, your Honor.

The Court: Do you have the newspaper

Mr. Sovern: It's three points your Honor.

[167] Mr. Landis: Well, Your Honor, the witness—

Mr. Sovern: Rather than offer the *New York Times,* I would like to do this, Your Honor. It seems to me that you recall that I asked in voire dire and Your Honor expressed a preference to have me raise question about these charts on cross. It is now clear to me that—

First of all, the failure to bring them down to date is a gross deficiency making it impossible for you or

any other tribunal reviewing this record to make an accurate record of the effect so I move at this time—I move at this time to strike the chart in supporting that.

The Court: Well, I might be disposed to make some comment on them if you can show me what the history of this spread has been since the terminal date on the chart.

Mr. Sovern: I respectfully—we have—

The Court: I mean, I'd be very frank to say that if these are chopped off at a certain date and then the subsequent history shows that the spread has narrowed so that it's no longer significant, then I would be inclined to say that the credibility of these charts to prove anything that the witness has been testifying about would be seriously undermined. T 165-3 to 167-25.

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[170] Mr. Laulicht: For the record, S-3 will be a two-page chart headed 1975 for the New York-New Jersey Ports, 6 per cent, 2008 and the [171] Massachusetts Ports, 6 per cent, 2011 covering the period January 3 through 23.

Mr. Sovern: I think the question I [put] to the witness is, are you familiar with the current—the January price spread between Massachusetts Ports and New York Port Authority bonds?

The Court: Then take a look at this particular document and see if it corresponds to your knowledge of what the prices have been for those issues during the month of January.

The Witness: The latest figures seems to be reasonably consistent with what I have observed in the market.

Excerpts from Testimony of John F. Thompson

The Court: The figures reported on S-3?
The Witness: Yes. T 170-23 to 171-15.

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[172] By Mr. Sovern:

Q. Now, you'll notice, Mr. Thompson, these numbers go down only to January 23rd; that, of course, is due to the time in which they were prepared.

You'll recall I asked you for the spread on May 10, 1974, before Governor Wilson's signature and you answered that the spread was five. Can you tell me what the spread was on January 23 in light of S-3? A. Yes. The spread is five that day. T 172-1 to 172-9.

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[178] Q. Do I accurately recapitulate your testimony, Mr. Thompson? You cannot account for short term changes in the spread between New York Ports and Massachusetts Ports. A. That is correct.

Q. Now as to the long term trend from May 10, 1974 to January 23, 1975 there is no change in the spread between those two bonds, is that correct? A. It happens that there is no change between those [179] two dates. But that does not necessarily show that it is a long term trend. There can be short term things happening in January which account for what happened in January.

Q. I asked you earlier, Mr. Thompson, what is the long term trend, and you told me seven or eight months so I picked the period that I thought met your specifications. A. One does not approach these things with academic rules. One judges them by experience and by what happens over a period of time. Taking the long term trend that is shown, sure, back in late October they came together for a time there too. Then they spread out again. We could very

Excerpts from Testimony of John F. Thompson

well be in a period just such as that now, where temporarily they pull together for the time being. I don't think that you can say that you establish a long term trend by picking the dates which give you the result you want. T 178-17 to 179-17.

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[180] The Court: Wouldn't it be fair to say, Mr. Thompson, that the selection of December 14 for [181] the purpose of preparing these two charts then might have been an arbitrary selection?

Mr. Landis: That was just the day that it was made, Your Honor.

The Court: Isn't that an arbitrary date then?

Mr. Landis: It was made at that point in time. They had asked us for the exhibit and we gave it to them.

The Court: I understood the witness to say, and I understood you to be re-enforcing his testimony, that if you just pick two dates, that that would not necessarily show a long term trend, because there might have been something else going on at that particular time which would affect the spread between the two bonds.

Mr. Landis: Yes.

The Court: It so happens that these charts that were prepared by you on December 14 also happen to coincide so far as the evidence I have before me now is concerned, with the maximum spread between the two bonds. And he has now shown evidence that subsequent to this date, this spread narrowed considerably.

Would you encompass what has happened after December 14 through February 3 of 1975 within the

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[182] long term trend? Which I take it is a period of some approximately seven weeks.

The Witness: Your Honor, when the long term trend has shown this widening over a period of some six, seven or eight months, and then narrows again in the course of one month or five weeks, this may not be conclusive as to what comes next.

The Court: We would be able to make a lot of money if it were conclusive.

The Witness: We would, and it could be somebody lost a lot of money. It could be somebody sold short through here and then covered in January.

The Court: All I am suggesting to you is this: If this chart—and I am taking 91 as the example—if this chart were continued out through February 3, 1975 showing a gradual narrowing of the spread throughout the rest of December, January and through February 3; would you say that that is deemed to be part of the long term trend with respect to the spread between these two bonds?

The Witness: No.

Mr. Landis: I think he has answered the question.

The Witness: I would be hesitant because of these other points that this has happened before, [183] Your Honor. May I point out, that, suppose for the sake of argument we accept the five point spread—incidentally, I looked up during the recess, my trade desk gave me a bid price of 82 on the Port of New York rather than 83 which is used in the paper here.

But if we take a five point spread and look back to when this all started, when there was practically no spread, that five points applied to at least a billion of Port Authority bonds issued under the

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covenant and amounts to 50 million dollars. That is quite a tidy sum. T 180-24 to 183-12.

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Q. Let me try it this way: Do you think these charts as amplified by the down to date material, reflect the impact of Governor Wilson's signature of repeal on the difference in prices between New York Ports and Massachusetts Ports? A. I don't think Governor Wilson's signature of repeal can be taken here as one sole event. T 183-18 to 183-24.

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[184] A. It is the sequence of events. And the whole process of repeal is reflected here. T 184-3 to 184-4.

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Q. Do I take it correctly that your answer is no that the charts cannot reflect that? . . . T 184-14 to 184-15.

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Reflect Governor Wilson's signature. T 184-23 to 184-24.

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[185] A. I think, counselor, that your view of relations of markets to events is much too automatic.

Mr. Sovern: I am asking you for your opinion.

Mr. Meyner: It is his opinion.

A. It is not a question on which I would feel that one knowledgeable in markets could give an opinion.

Q. Then the charts do not reflect it. If you gave me an opinion—A. The charts are not supposed to reflect one event. T 185-8 to 185-16.

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[188] Q. Do you have an opinion on the basis of the exhibits dealing with the prices of Massachusetts Port

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Authority and New York Port Authority, all of the exhibits, dealing with that subject, do you have an opinion as to whether the spread between the New York Port's and the Massachusetts Port's was affected by Governor Wilson's signature of the repeal legislation? A. Was it affected? Now, you have left out of the question the current spread. I think Governor Wilson's repeal was one of the events in the course of repeal which affected the general trend of the market, yes. T 188-5 to 188-17.

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[189] Mr. Sovern: The witness has declined to answer the question, whether the exhibits you have introduced as amplified by the exhibits we have introduced permit him to have an opinion as to whether the spread between these two bonds was affected by the signature of Governor Wilson.

I recall that on direct testimony, he said he knew of only, of no other facts that would spread the market except repeal by the two Legislatures and signature by the Governors. That was the testimony and I am cross-examining as to whether he has— T 189-1 to 189-13.

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Q. Now, we are asking you about one of the only facts that you thought had an effect on the price and I am asking you whether you wish to change your testimony in that respect. A. No, I do not wish to change my testimony.

Q. Then do you have an opinion as to the effect of Governor Wilson's signature on the spread in price between the Massachusetts Port bonds and the New York Port bonds? T 189-17 to 189-25.

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[190] A. As I have stated, my opinion that relates repeal of the covenant to the market on Port Authority bonds combines the series of events which occurred in that and I do not think anyone professional in the market would try to tie a market trend to one of those events separated from others.

Mr. Sovern: Your Honor, I respectfully submit the question is susceptible of a yes or no. It asks whether he has an opinion and I respectfully ask—

The Court: Do I interpret your answer to be you do not have an opinion with respect to that particular event having such an impact on the market?

The Witness: Yes, I think it is fair to say that I do not have an opinion as to that particular event and I do not think that an opinion on that point is something that would be professionally looked upon as knowledgeable in the market. T 190-6 to 190-24.

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[211] Q. I call your attention to Page 1 of this D & B report [Exhibit P 1], Mr. Thompson. You'll find that this is the offering—this credit report is occasioned by the imminent sale of the 19th series? A. Yes.

Q. Did the 19th series contain a covenant? A. No, because the covenant had not then been passed by the two legislatures.

Q. Was a special premium paid by the Port Authority for the sale of the 19th series? A. Not so far as I know. It was a $25 million issue. It was not large in connection with the Port Authority financing.

Q. All right. Now, the Hudson-Manhattan legislation was introduced in New York and then cleared the second

Excerpts from Testimony of John F. Thompson

house of the New York legislature on March 25, 1961. Governor Rockefeller signed it on April 6, 1961. I stated that for background.

Would you expect the price of Port Authority bonds to be affected by this action during the period, let's say, from the beginning of March to the middle of [212] April? A. This is 1961 you're speaking about?

Q. 1961, the period during which you were concerned and I take it what you were concerned about was Governor Rockefeller's indication that he wanted Hudson & Manhattan picked up by the Port Authority. A. And your question again is?

Q. Would you expect this—I wouldn't—would you expect the legislature's actions and Governor Rockefeller's signature of the legislation requiring—directing the Port Authority to take over the Hudson and Manhattan without a covenant—this is 1961—not [1962]—would you expect that legislation to have affected the price of the bond? A. I think probably not because this was a step along in the discussion and development situation.

Q. Okay. I call your attention now, Mr. Thompson, to P-4. This is the draft of your speech that I guess was never actually delivered as a speech. T 211-5 to 212-18.

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[213] A. Yes. It was not intended to be a speech. It was a draft for internal discussion purposes in considering the question of what some of us in the investment community could do to help in the situation where the Port was being pressed to take on more and more in mass transit and there was the covenant; to see whether there were ways of accommodating to the covenant and still doing something in mass transit.

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Q. And one of the ways you discussed was by possible bondholder consent to modification? A. I discussed bondholder consent, yes.

Q. And in your view a meeting of the holders of consolidated bonds would have had to be held in order to modify the covenant? T 213-1 to 213-14.

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A. This is not my opinion. This is what was provided [214] in the consolidated bond resolution.

Q. Is that—let me ask the question. It may be that Counsel may answer it.

We received these documents [with] some attachments or at least they seem to be together in the file; one of which was section—a Xerox copy of Section 16, the modification section. Is that the section to which you're referring? A. Yes. That I believe is attached to the copy I have here.

Q. Now, under that provision as you understand it, there would have to be a meeting of the bondholders. Would there have to be a quorum at that meeting? A. A quorum of 60 percent and any variation would have to be approved by the holders of 60 percent of the bonds then outstanding adjusted for anything that was in the sinking fund and all that sort of thing.

Q. I take it you were relying on Section 16b, would I be correct in that? A. It's been some time since I read this—

Q. Please take your time. A. —Counsellor.

Yes, I think so.

Q. Now, as you look at that provision, I take it that 40 percent of the bondholders may have their rights altered by 60 percent of the bondholders. Is that [215] correct? A. That's what's provided in the resolution, yes.

Q. Are there any exceptions to the extent to which the 60 percent vote may impair the obligation of the bonds being held by the other 40 percent?

Mr. Landis: Your Honor—

A. I would have to read it fully again but I'm sure one exception is that the interest rate can't be reduced or the maturity changed.

Q. Would you focus on the proviso of Paragraph B and if you read that perhaps that would be helpful. A. Just before the small "i" you mean?

Q. Yes. If you'd read that aloud. A. "Provided that no such amendment or repeal or modification shall alter or impair the obligation of the Authority which is absolute and unconditional to pay the principal and interest of any consolidated bond at the time and place and at the rate or amount and in the medium of payment prescribed therein without the express consent of the holder of such bond."

Q. So that there are several promises made by the Port Authority that cannot be taken away from the bondholders. Is that correct? A. Yes. This is customary in this sort of provision.

Q. In any event, it was your opinion that the [216] approach to the bondholders would fail. Is that correct? A. Yes. Certainly, unless some very substantial quid pro quo were offered and none has ever been suggested.

Q. The way you put it, as I recall—not as I recall it, as I read it is that even if the approach were made with a moderate increase in the interest rate, it would be unacceptable. A. With a moderate increase I then believed that it would be unacceptable and I still do.

Q. Now, you stated— A. A moderate increase being—I was thinking of the Triboro thing where it was a quarter

of one percent, perhaps half of one percent. I'll define moderate for you. T 213-1 to 216-13.

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Q. Now, as you told us, this draft was an effort to find the way to deal with mass transit without repeal of the covenant. You explored one track, modification, found that likely to be unavailable.

[217] You then offered another alternative, did you not, on Page 4, second paragraph—second full paragraph? A. Well, this is the proposal—the tentative proposal which all of this was being a draft memo, you can understand, of an override toll enacted by the two states, not by the Port Authority and I went on to qualify this somewhat because at that time I felt that that increase in the toll might reduce the traffic and that that might really impair the bondholders' rights to the normal increase in traffic and that therefore some of that should go to them, but this was all a tentative notion which came to naught.

Q. Were you concerned that the security of the bondholders would be damaged by your proposal? A. I was trying to figure out something where it would not be damaging.

Q. You stated on direct that you were subsequently advised that this posed problems of interstate commerce and possible Constitutional objections. Who gave you that advice? A. Well, some of it—some of the municipal bond counsel that I know and have talked to so many of them that going back, I'm not sure which ones.

Q. This was informal rather than retained counsel? A. Oh, yes. This was an informal discussion. T 216-22 to 217-25.

[220] Q. Your letter to the *Times* has a similar proposal. A. Somewhat, broadened.

Excerpts from Testimony of John F. Thompson

Q. Was that because you got some advice and decided to be vague about it? I'll ask the question. Was the difference between this document and the *New York Times* letter attributable to your receiving such advice? A. Not entirely. It is attributable in part to thinking about this proposal for a couple more years and trying to mature my thoughts, and realizing for one thing, that the concern, which is to get some money here, is apt to be for the New York Subway System, and any idea that you could do something like that with a tax only on the crossing between here and Manhattan and without touching the other entries into Manhattan would be ridiculous, and I'm sure any Governor of New Jersey would soon find it so. T 220-1 to 220-17.

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[221] Q. You say in your draft that your plan could be accomplished within the present framework in covenants with the bond holders. Is that correct? A. I then thought so, yes.

Q. Do you now think so? A. There was some statement made then that indicated that there was a divergence of legal view on that, and I would have to respond simply that there was a difference of opinion on that point.

Q. You testified at some length as to the meaning and the effect of the 1962 covenant.

> Mr. Landis: Your Honor, I don't think that is correct. I object. He testified as to his understanding, not—I don't think he purported to be an expert on the meaning, and we did not offer him as such with respect—he testified that the salesmen and others relied on his interpretation of the covenant, and he testified as to how and in what respects; it was more precise than Section 7 of the bond resolution.

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> The Court: I don't think we need to get too far into that, but I will permit you to ask the question.

Q. Doesn't your proposal violate the 1962 covenant, Mr. Thompson [222] A. Which proposal?

Q. Your proposal in P-4 beginning on page 4, the [toll] override. A. I have already said that that was the discussion proposition, that I had long since moved away from; I don't know whether it violates the covenant.

Q. You don't know whether it violates the covenant? Is that your testimony?

> The Court: He just said that.
> Mr. Landis: Yes, he just said that.

A. At the point of discussion of it, there was a difference of opinion. That is my answer.

Q. Is there still a difference of opinion as to the compatability of your proposal with the covenant? A. Counsellor, I regard that proposal as two to three years old and quite passe. I doubt if anybody else has thought of it in the last two and a half years.

Q. Do you know the date on your *New York Times* letter? May 1st, 1974, is that correct? A. I don't have it before me, but it probably is. T 221-1 to 222-20.

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[223] Q. I call your attention to the next to the last paragraph, the third sentence in which you say: "A broad view of urban and energy problems suggests that government should act to discourage auto traffic into major cities in favor of the greater use of mass transit. This would probably involve a sizable shifting of funds from charges imposed on automobile traffic to the support of mass transit. To do this is an exercise of the state police power, and

Excerpts from Testimony of John F. Thompson

should be done by the two states themselves and applied to all automobile traffic entering Manhattan." That is within the last two and a half years, is it not? A. Yes. That is not the proposal I made.

Q. Is this proposal compatible with the 1962 covenant? A. I think it could be so arranged, yes.

Q. How would you shift charges imposed upon automobile traffic crossing the Hudson from automobile traffic for the support of mass transit? A. I presume that would be part of it.

Q. How would you do it, consistent with the 1962 covenant? A. I think I have said that it was an exercise of the state police power; and the *Times* incidentally left out the phrase and taxing power that I had it in the letter that I [224] sent.

Q. I have seen that draft, and you accurately describe it. A. It seems to me that it is up to the states to take action here under their authority, if they want to do it. T 223-2 to 224-5.

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[225] Q. How then, Mr. Thompson, would you follow through on the proposal made in your New York Times letter, without violating the 1962 covenant? T 225-1 to 225-3. A. Well, the 1962 covenant deals with Port Authority revenues and funds. This suggestion, while it might conceivably use the Port Authority as a collection agency on cars going through the tunnels and bridges, still would be something imposed by the states; it might be done simply by a tax levy through the City of New York on all vehicles coming into the city. They might have to buy a sticker to come into the city. There are a variety of ways it could be done, and it would not necessarily flow money through the Port Authority funds that are pledged to the General

Excerpts from Testimony of John F. Thompson

Reserve Fund. In fact, the intent of the proposal was that it would not.

Q. Among the possibilities you contemplate, though, was a tax on automobiles at point of entry. A. That would be one way to handle it, yes.

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[227] Q. Where would a charge imposed on traffic entering into Manhattan be imposed?

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A. I would not consider these tolls. They would be, if you will, taxes on the privilege of coming in.

The Court: Wouldn't you consider that an agreement between New York and New Jersey, Mr. Thompson, or legislation by those states which [228] set up a taxing facility as far as entering into New York from New Jersey would impair the basic covenant—forget about the 1962 covenant—but would impair the basic covenant between the states and the bond holders?

The Witness: No, I would not consider that.

Mr. Sovern: Can I call the witness' attention to the Official Statement at page 28 dealing with rate powers and covenants? • • •

Q. You will find in the first paragraph references to legislation including the covenant, that the two states covenant with each other and with the bond holders that the two states will not diminish or impair the power of the Authority to establish, levy and collect tolls, rents, fares, fees or other charges in connection with any facility owned

or occupied by the Port Authority. Does that affect your— A. I did not consider the idea affected that power. Perhaps legal counsel would dispute this and want to argue it out. But it did not seem to me action by the states on their own behalf and entirely supplementary to the revenue producing ability of the Authority which is here described would impair the authority's power.

[229] Q. Mr. Thompson, if the Port Authority raised the toll on the trans Hudson bridges and tunnels to one dollar and gave the extra fifty cents to mass transit, pursuant to legislation, that would be a plain violation of the covenant, would it not? A. I believe it would, yes.

Q. It would also be a violation of the consolidated bond resolution and each bond resolution. Is that correct? A. Yes.

Q. But you said they can without violating the covenant or any other protection, direct the Port Authority in the exercise of the police and taxing power to collect 50 cents a car for them. Is that correct? T 228-12 to 229-14.

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A. I believe that the states could and that the Port Authority would not be involved in the transaction, except possibly as an agent for the collection of the sums would be separated.

Q. Which do you regard as more inimical to the [230] bondholders' security, your proposal or the repeal of the covenant? A. Obviously the repeal of the covenant.

Q. You testified on direct examination, Mr. Thompson, that the effect of the repeal on other bonds was a serious matter. A. Yes, sir.

Q. And you testified, did you not, that if Governor Byrne had recommended repeal, never mind enacting it, but recommended it before the sale of the Sports Authority bonds,

that the bonds would have been unsaleable. Is that correct? A. I would so testify, yes, sir. T 229-21 to 230-13.

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Q. You also testified New York Power Authority bonds had suffered in their marketability because of the repeal. A. I did, sir, yes.

Q. New York Power Authority bond holders have nothing at risk from mass transit. The repeal of the covenant does not affect the value of their security. [231] Is that correct? A. Well, as far as subjecting them to the hazards of mass transit, it has nothing to do with their security. As far as indicating that the state of origin might revoke and not abide by something that is in their promise to pay, they have a great deal at stake.

[232] Q. So it is a fact that the state has broken its promise that impairs the market ability of power authority bonds? A. Yes, that's correct.

Q. And even though the specific promise broken has nothing to do with the security they have? A. I presume that is correct, yes.

Q. So the same could be true of Port Authority bonds to, could it not? A. I don't follow you, would you rephrase that?

Q. That market is reacting to the fact, if it is reacting at all, to the fact that the state has broken its promise, that it is a matter not of concern about impairment of security. It is concern about the reliability of state promises? A. Well, that certainly is true of the indirect affect on other things. In the case of the Port Authority it has broken its promise to Port Authority bond holders and I don't see how you can separate them.

Q. We don't need to separate them. I take it it is your testimony that the mere fact of breaking of the promise,

irrespective of any security interest would diminish the values of securities issued by New York and New Jersey and its agencies, including the Port Authority? [233] A. Yes, and indeed it has.

Q. I call your attention now to the exhibit marked P-3, a memo by you to Mr. Morton. T 230-19 to 233-3.

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Q. I call your attention to the first sentence, the provisions of section 6 quoted above are part of the contract with holders of bonds issued between March 27th, 1962 and May 10th, 1973.

Were any series of bonds issued after May 10th, 1973, and before the date of your memo? A. Yes, I believe there were two series of bonds issued in that period.

Q. I take it that the implication of your sentence then is the provisions of section 6 were not part of the contract with the holders of those bonds? A. That's correct, yes.

Q. I call your attention to page 4, first paragraph, same exhibit, next to last sentence.

Would it be a fair paraphrase of your view expressed there to say that the investment status of consolidated bonds would be materially impaired unless the Port Authority's incursion in the mass transit field is limited? T 233-5 to 233-23.

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[234] A. Yes, I think so.

Q. [Would] the members of the financial [community] agree?

The Court: If you know.

The Witness: I don't know how to answer that, your Honor. I have not discussed with other members of the financial community your paraphrase of my language so I don't know how to answer it.

Q. You have indicated to my satisfaction that you regard my paraphrase as a fair statement of your view expressed here. I ask you only if your view expressed here was shared by other members of the financial community?

The Court: As you stated it.

The Witness: Yes, I think the financial community realized how little of the net [235] revenues of the Port Authority might conceivably be made available for mass transit if something like that were put through and also therefore extremely concerned about statements of one-hundred-million dollars a year and other things which are entirely out of context of the Port Authority's actual finances.

The Port Authority's net revenues are good for an enterprise the size of the Port Authority, but compared to the mass transit problem, they are peanuts.

Q. There is no legislation pending or gubernatorial proposal to have the Port Authority take over all mass transit, is that, Mr. Thompson? A. Frankly, counsel, nobody in the investment community can tell what the proposals are of those who want repeal. That is one of the unfortunate uncertainties of all of this. It is just destructive and not constructive. T 234-9 to 235-20.

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[239] Q. Tell me now, Mr. Thompson, whether you think a municipal bond could be sold if it was sold with an explicit stipulation in the official statement stating that the State of which the municipal agency is a part reserves the right to modify covenants and provisions affecting the operation of that agency if sufficient public need required? T 239-4 to 239-9.

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Excerpts from Testimony of John F. Thompson

[240] A. Yes, I think it would be difficult to sell such an issue.

Q. You would have to pay a premium for floating such an issue, I suppose. A. If it were saleable it would carry a very high interest cost. Premium is a different word in market parlance. It involves the price factor.

Q. I understand. Thank you. If that is the case why weren't investors paying something more for New York Port Authority bonds when according to your testimony they were under the impression that its covenants could not be modified, whereas an informed investor would have to know that the Massachusetts Port Authority bonds covenants could be modified? T 240-2 to 240-15.

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[241] The Witness: At what point in time?
Mr. Sovern: In April 1974.
The Court: Or prior thereto.
Mr. Sovern: Or prior thereto.

A. I would think that the question never arose in an investor's minds as to the Massachusetts Port Authority. As I said yesterday there was a set of circumstances there which made entirely impractical the sort of drive to get money for mass transit which we have seen here. So the question just does not arise and it is not a real question. T 241-16 to 241-25.

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[244] Q. I'd like to call your attention [245] now, Mr. Thompson, to plaintiff's exhibit 5, your letter. T 244-25 to 245-2.

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Q. That is your letter to Norman Hurd of June 10th, 1974. I call your attention particularly to the final paragraph on page 1. What did you have in mind there when you said that there would be a continued effort in the investment community working with the Port Authority to further [246] its involvement in mass transit within the covenant including the possible request for bondholders consent to a change? A. I think the sentence should be read in connection with the sentence which follows which was if the repeal bill is signed, if the repeal bill is signed. However, all of this potential effort will unfortunately have to be channeled into the mobilization of investors to uphold the covenant in the long constitutional court battle which will ensue. T 245-20 to 246-11.

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[247] A. If you wish me to answer further as to what efforts were going on, I think some efforts were indicated in some of the things we went through yesterday, and some of the memos I wrote, there had been discussion that I knew of with a good many people in the investment community as to how something could be worked out. There has been discussion with Port Authority people. The Port Authority itself presented to the two governors and the governors adopted it, a program involving further involvement in mass transit within the covenant. All of that is now stymied just as I've said it would be.

The Court: What sort of a change in the covenant would you have anticipated the bondholders would consent to?

The Witness: The bondholders [248] might consent to a change which would permit funds that flow to the final reserve fund a consolidated reserve fund to be devoted to this in return for an increase in the interest rate which would be substantial.

Now, I said in one of the memos that quotes were taken from yesterday, that a moderate increase would probably not attract bondholders. And this would not be an easy thing to do, your Honor, but in the long run my opinion was that an attempt in that direction, first an attempt in the direction of doing as much as possible within the covenant. Secondly, if it were then necessary to look for a change agreed to by the bondholders because on that basis, there would be specific proposals. There would be something that would be measurable. There would not be this feeling—just an outright repeal of the covenant—there is an attempt to get money way high on the operating revenues of the Port Authority, which would really impair it. An approach to the bondholders [249] would be in terms of specifics for so much of an application of surplus funds for mass transit might be allowed. But, as I say, that would be the second choice in my mind.

By Mr. Sovern:

Q. It would be fair, would it not, Mr. Thompson, to say that you regard the obtaining of bondholder consent under the conditions set forth in your memorandum as an exceedingly difficult undertaking? A. It would be an exceedingly difficult undertaking and it would have to be, to have any hope of success, it would have to carry substantial benefits to the bondholder in the way of additional interest.

Q. Now, you referred to other plans going forward at the Port Authority to help mass transit within the covenant. A. Yes, sir.

Q. Can you be more particular, more specific? A. The program to extend PATH to the Newark Airport and on

to Plainfield, and the program to—that involves a number of railroad connections, so, I think, in this area, which I can't draw a [250] map of, but there were several of them permitting the flow of mass transit into Penn Station, which is not now possible, and the connection to Kennedy Airport in New York from Penn Station.

[251] Q. Do you have any idea how long those plans have been under consideration by the Port Authority? A. For several years, I don't know exactly.

Q. Do you know whether the Port Authority has certified within the meaning of section 7 that it would not impair the obligations to the bondholders to undertake that enterprise? A. The program calls, as I understand it, for assistance from both state government and from the federal government. These have not all been received. I believe it has been said that there was an expectation of such help from New Jersey which was later denied, so, now, the Commissioners have not yet certified the program.

Q. Do you know what fare levels would have to be set in order to meet the terms of the covenant in order to have those plans go forward? A. No, I don't think any study has ever been presented that brings it down to fares.

Q. Are you familiar with an occasion on which the Port Authority Commissioners refused to go forward with the Plainfield project unless a [PATH] fare increase was approved? A. I don't think I am specifically, no.

[252] Q. It occurred on February 19th in an effort to refresh your recollection, if it is the case, the time involved would have been February 19, 1974? A. I probably was aware of it at the time. It seems a perfectly logical arrangement. I presume the extra fare was needed to obtain the degree of self-support required. T 247-10 to 252-8.

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Excerpts from Testimony of John F. Thompson

[253] Q. I call your particular attention [254] to the paragraph [of Exhibit S-5] beginning with the bottom of column one of the letter in which Mr. Ronan says—he is referring to the time when he approved the—he stated the repeal would be welcome.

"I have also stressed that the lifting of the statutory covenant, per se, does not mean that bondholders' security would be eroded. The two states have not determined and the Commissioners have not acted to impose deficit burdens on the Port Authority in rail or other fields, which could impair revenue coverage or reserve requirements established in our indentures.

"Additionally, the Board of Commissioners is committed to preserve the credit of the Port Authority which is vital to the present and in any future undertakings of the agency.

"Governor Byrne on signing the New Jersey bill expressed his own determination to avoid impairing the Port Authority's credit."

Would you indicate for us which, if any, portions of that paragraph with which you disagree. A. May I request if another letter that was put in evidence yesterday which was my private reply to Commissioner Ronan which incorporates my then [255] views and I am sure will also incorporate my answer to this question.

The Court: Well, I think the question really is do you agree as you are sitting here today with the statements made by Mr. Ronan's letter?

The Witness: Your Honor, the letter I wrote to him was one in which I had given that question a great deal of thought.

The Court: What number was that?

The Witness: P-14. And I think the first paragraph of this letter is appropriate as an answer to your question, leaving out the sentence about the conciliatory tone, "Your personal assurances about the Commissioners' intent to maintain Port Authority credit standing were well-stated. However, the best of intentions are not apt to be persuasive to investors who have just experienced unilateral revocation of an important part of their bond contract.

"Furthermore, if the assurances are to be accepted at face value, it is [256] difficult to understand what is to be gained for mass transit by repeal of this covenant."

That would be my answer to your question.

Excerpts from Testimony of John F. Thompson

Q. You left out the first sentence, "The conciliatory tone of your May 9th response to my letter of May 7th, *New York Times,* is welcome."

Do you recall your testimony yesterday in which you indicated on page 91 of the transcript—the Court had asked you was the investment community equally shocked, the equal being to Governor Byrne's—was the investment community equally shocked [when] the then Governor of New York—this is on page 90, line 24, "advocated repeal and the New York Legislature actually voted the repeal?"

Your answer, "I think to say 'equal shock' would be unfair, your Honor. Let me see if I could explain it. When Rockefeller signed the repeal in 1972, he issued a statement which in its terms was very conciliatory. It had words, 'If it is, like I should be conferring with the Governor of New Jersey to try to work out something here that would not impair the credit of the Port [257] Authority.' It was a less final thing." A. And your question is?

Q. Well, the conciliatory Rockefeller message is regarded as quite important; the conciliatory Ronan message is regarded as worthless. Is that correct? A. The concili-

atory Rockefeller message was issued along the way while the process of repeal was uncompleted. It had to be adopted by New Jersey. It indicated that steps might be taken to do something modifying—more moderate than the repeal.

Conciliatory, there is a word that looks forward to constructive action. Conciliatory here is simply that the tone of his letter which happened after the repeal had been finally concluded or was about to be.

Q. In other words, your answer on page 91 says, "It had words in it like, 'I shall be conferring with the Governor of New Jersey to try to work out something here that will not impair the credit of the Port Authority.'"

When you said that, do you mean that you thought Governor Rockefeller was going to try to induce Governor Cahill not to go along with the repeal? [258] A. No, I thought he was going to talk to Governor Cahill probably sensing that Governor Cahill was opposed to repeal and try to work something out, perhaps along the line of what eventuated, which was the repeal of the covenant applying only to future issues.

Q. And that is why he signed repeal of a wholly different statute in New York? A. Well, he had other reasons. His statement is much longer than that, to be sure.

Q. But he did sign the repeal? A. He did sign the repeal, yes.

Q. You were not troubled after that because he was conciliatory after signing? A. I would never say that. I hoped—I was not troubled by it.

Q. It was less shocking? A. I think I tried to explain the matter as I said yesterday, of shock. I thought I made the point. The shock came from the time that this was an action by a Governor of New Jersey whereas on the

previous occasion, the then Governor of New Jersey had been the bulwark who stopped repeal.

That was the basis of my use of the word "shocked."

[259] Q. Let's see then, you were shocked, tell me if I correctly capture of essence of your testimony: You were less shocked by the Rockefeller signing of the repeal because he wrote a conciliatory statement upon approving repeal and because the process of repeal was not yet concluded, the New Jersey Legislation having not yet been enacted, indeed never been enacted. That is correct.

All right. Now, we are in 1974, Mr. Ronan has written a conciliatory letter and the Governor of New York has not yet approved repeal, but you and your colleagues in the bond market, I think it is fair to say, are behaving in a way that regards him open to persuasion on veto.

Why was not this Ronan conciliatory letter important? A. Because, conciliatory there applied only to tone. It did not apply to anything that suggested Commissioner Ronan would change his position.

Commissioner Ronan had taken a position in favor of repeal.

Q. Governor Rockefeller had not? A. Governor Rockefeller had taken a position favorable to repeal. Governor Wilson had not yet, although it was beginning to be widely believed, [260] would sign the repeal and we were doing everything we could to dissuade him.

Q. I would like to return to that same paragraph, the first sentence says—

The Court: This is S-5?
Mr. Sovern: Yes.
The Court: Do you have S-5?
The Witness: Yes.

Q. This is Mr. Ronan:

"I also stressed the lifting of the statutory covenant, per se, does not mean that bondholders' security would be eroded."

Do you agree with that statement? A. No, sir.

Q. The next sentence says, "The two states have not yet determined and the Commissioners have not acted to impose deficit burdens on the Port in the rail or other fields which could impair revenue coverage or the reserve requirements established in our indentures." A. They have not acted because they could not under the covenant. The covenant was then still in force.

Q. Could they act now? A. Your Honor, that calls for a legal opinion, [261] I am afraid.

The Court: No, it is based upon your understanding of the consolidated bond resolution reserve requirements, the statutory reserve requirements, all of which I assume were matters of your personal knowledge prior to the enactment of the covenant because you were dealing with these bonds before the covenant was ever enacted.

The Witness: I think if they acted now to impose deficit funds on the Port Authority in the rail or other fields which could impair revenue coverage—

The Court: Or reserve requirements?

The Witness: —or reserve requirements, there would be an additional lawsuit filed on the same ground that are present in this suit. This would be my understanding.

The Court: But there were still protections which the bondholders had without the covenant if the Commissioners of the Port Authority acted in such a manner [262] as to impair the revenue coverage or

the reserve requirements pursuant to which the bonds had been issued?

Mr. Landis. I do not think that was the context of the question. My recollection was the question was asked in the context of repeal and this covenant.

The Court: I am saying—

Mr. Landis: After it had been repealed, whether now they could do it? The witness answered he does not know what the legal situation is.

The Court: Mr. Landis, please, if that is an objection, it is overruled.

Now, the covenant has been repealed, presumably the bondholders are back to where they were prior to the enactment of the covenant in 1962.

You are dealing with those bonds in the period prior to the enactment of the covenant and I assume you were familiar with what the protections were that the bondholders had before the enactment of the covenant and I think the question was could the Commissioners have, or do you [263] agree with the statement of Mr. Ronan that, in effect, the Commissioners could not impair the reserve requirements or the revenue coverage under the statutes and resolutions in effect without the covenant if they would do so today or attempted to do so?

The Witness: As I read Mr. Ronan's statement, your Honor, it is to the effect that the Commissioners had not acted and I think the question directed to me was whether I agreed with Mr. Ronan's statement.

[264] Mr. Sovern: There was another question following it.

The Court: There was another question which followed it. Could they?

Excerpts from Testimony of John F. Thompson

Q. You said they could not because of the covenant, and I asked you whether they could today? A. My answer was that they could try, but I think that they would be brought into Court under the covenant.

The Court: Under the covenant?

The Witness: Yes.

The Court: Which covenant are you referring to?

The Witness: The 1962 covenant forbidding taking on a deficit rail mass transit on the grounds that repeal would impair the constitutional rights of the bondholders.

The Court: Let's forget about mass transit for the moment. Let's say the Port Authority decided it was going to build another World Trade Center, maybe the Moon Center, and they projected a cost of one billion dollars and knowing what the market conditions are today, and certainly there is nothing in the covenant which precluded them from undertaking such a venture, is that correct?

[265] The Witness: Nothing in the Section 7.

The Court: So all the bondholders would have as protection would be the Consolidated Bond Resolution requirements, the Certification, the 1.3 test and the general refunding bond statutory reserve requirements.

Mr. Meyner: I think you omitted something your Honor, must have State legislation of both States.

The Court: Yes, we are assuming the States have concurred in permitting them to go ahead with the venture; and let's assume that the bondholders decided that it would impair the credit of the Port Authority and impair the reserve requirements and the revenue coverage requirements; wouldn't the

Excerpts from Testimony of John F. Thompson

bondholders be able to go into Court to enjoin such action by the Commissioners and the State?

The Witness: I am not sure whether the hypothesis includes the Commissioners having adopted this.

The Court: Yes, that the Commissioners have adopted this.

The Witness: And they have certified it?

The Court: They made the certification.

[266] The Witness: Under Section 7 and whatever certification they need to do on the 1.3 test.

The Court: Yes.

The Witness: Well, the question that would arise I believe under the 1.3 test, and it might arise under the very extreme example which you have given—that is a lot of money.

The Court: If they built one, they can build another one.

The Witness: Under the very extreme example you have given the 1.3 question might arise, and it might be that the Port Authority would be unable to get bond Counsel to give an opinion that bonds could be legally issued at that time.

The Court: Well, that was not the question. Wouldn't the bondholders be able to go into court to challenge the certifications made by the Commissioners as to the various requirements that must be met before they could proceed with such a project?

Mr. Landis: With all due respect, your Honor, I object to the form of the question. I think it asks the witness whether some people can bring a suit. We all know that anybody can bring a suit at any time. If it asks him whether [267] the suit will be successful or not, I think it clearly asks for a legal opinion.

The Court: I want to try to find out what his understanding is of the protections which the bondholders had under the terms of the covenant and the prior statutes.

The Witness: Under the—

The Court: Under the Consolidated Bond resolution—

The Witness: Section 7.

The Court: That is right, and the prior statutes.

The Witness: Your Honor, I don't believe a legal question could be raised under Section 7. If the Commissioners certify that the project will not substantially or whatever—

The Court: Impair the credit.

The Witness: —impair the credit of the Authority, I doubt—here again, I am afraid I am expressing a legal opinion—I doubt that that could be contested. I would presume that their finding would be final in that respect.

As far as the 1.3 is concerned, the answer I gave you is the way I think a legal problem would arise. And I am very serious about that [268] because one of the most important facts at issue regarding the issuance of municipal bonds of any kind is getting a proper legal opinion from a recognized firm that these bonds can be legally issued. And if they could not indeed comply with the 1.3 coverage test, then as I understand the consolidated bond resolution the new bonds would not be legally issued. And I don't believe—if I may go further, I don't believe that existing bondholders would have any other way to get at it that I know of.

The Court: Is it your understanding that bondholders could never go into Court with respect to

any undertaking of the Port Authority, to challenge the validity of the statistics or figures relied upon by the Commissioners as the basis for the issuance of bonds for new facilities?

The Witness: It seems to me sir that the Section 7 findings by the Commissioners would be final. Again I am not a lawyer.

The Court: No.

The Witness: I am not sure of my answers here. And I think the legal problem on the other arises in a different manner. It might be then that—

[269] The Court: Let's say the Commissioners got a set of figures from a consultant. All right?

The Witness: That's right.

The Court: And that is before them when they act to approve the project and the issuance of the bonds; and the Bond Counsel then issues his opinion that the bonds are legal issues. All I am asking you is what your understanding is of the 1.3 test. Let's bring it down to that.

The Witness: The legal opinion has been issued?

The Court: Yes, the legal opinion has been issued based upon the statistics and the projections which the Commissioners have in front of them when they approve the issue; is it your understanding that the bondholders could never in any forum challenge the validity of the projections which were made.

The Witness: Yes sir, that is my understanding.

The Court: Then let me go to the next step. If that is the case, now supposing the Commissioners have before them a mass transit project with a set of figures prepared by Joe Doaks, whom they recognize that the investment [270] community would never

accept as a qualified statistician, and they approve a mass transit facility and they certify that it is self-sustaining—all right?

The Witness: Yes.

The Court: —and again they made the certification; are you saying that the bondholders—now we are operating within the covenant—are precluded from coming into Court and challenging the validity of the statistics which formed the basis for the Port Authority's actions?

Mr. Landis: For the record, your Honor, I know what your feeling is, but I wanted to note that I would object to this line of questioning. This clearly is asking the witness for a legal opinion.

The Court: No. I want to know what his understanding of the covenant is now.

Mr. Landis: I think in the context of the way the question is asked, it clearly asks for a legal opinion. I do not press the point because I know what your position is.

[271] The Witness: Your Honor, on that point I'm not sure at this point. I would think there would be more chance of a contest there, bringing a suit there than there would be on any of the others.

The Court: Well, we are dealing with objective facts now.

The Witness: Yes, yes, that's true.

The Court: There is the 1.3 test, the mathematical test that must be applied based upon the criteria which are set forth in the resolution, and in the covenant you are dealing with a certification that the project is going to be self-supporting. Well, again, we are dealing with a mathematical test, the projections which are made, do they show that the project will be self-supporting.

Mr. Landis: Your Honor, do I understand that you are saying that the tests are the same, the 1.3—

The Court: No, I'm saying they are both objective tests.

Mr. Landis: But they are entirely [272] different tests. I think the record indicates that already.

The Court: They are different tests, I understand, but both are based upon projections of revenues.

Mr. Landis: Now, the 1.3—

The Court: And costs.

Mr. Landis: Now, the 1.3 test is historical revenues, in the first instance is historical revenues.

The Witness: Your Honor, I feel that this is a legal problem, and I certainly don't have a conclusive opinion on it.

The Court: Okay. What I am leading up to is this: Doesn't the investment community with respect to the acceptance of an Authority's bonds as proper investments really look to the integrity of the management of the particular Authority? And to the past performance record of the issuing Authority, the expertise of its staff, and so forth, as much as they do to a specific covenant or undertaking? Isn't that just as equally as important, if not [273] even more important?

The Witness: It certainly is very important and an exact equation, I would—

The Court: You may not be able to weigh them one against the other.

The Witness: But both are very important, and certainly the record of management, and I might say

that the record of management can become a very broad thing in a bi-state agency of this sort, including the appointive powers of the Commissioners, the influence of the governors and the Legislatures of the two states, all these things become part of the way of the record of management.

The Court: Yes, without any question.
All right, I'm sorry.

By Mr. Sovern:

Q. To be sure I caught the full import of your response to the series of the Judge's questions, is it accurate to say that of the protective covenants we have been talking about, to wit, Section 7 certification and the 1.3 tests and the mass transit covenant, of those three, the [274] mass transit covenant is the only one you feel confident entitles the bondholders to suit?

Mr. Landis: Your Honor, I have an objection. I don't think that was his testimony at all.

Mr. Sovern: If it isn't he can say so.
Excuse me, your Honor.

A. Feel confident is too strong.

The Court: Yes.

A. (Continuing) It is the only one where I think there is some possibility. Not being a lawyer and not being sure there is, I think, some possibility of bondholder action.

The Court: A better possibility than with respect to the others?

The Witness: A better possibility than with respect to the others.

By Mr. Sovern:

Q. And that would be a major reason for attaching importance to it, is that correct? A. A major reason?

Q. For attaching high importance to it. A. Yes, that would be an important reason.

[275] Q. Now, I'd like to come back—

The Court: Well, I take it that the reason for that is that if the covenant as such is not enforceable in a court, aside from the action of the marketplace, then it is really meaningless, it is worthless?

The Witness: Yes, it was certainly sold to investors as a legally enforceable contract.

Q. Now, I come back to my question with respect to S-5, the paragraph under discussion, the second sentence: The two states have not determined, and the two Commissioners have not acted, et cetera, and I asked you whether they could, and you said they could not so act because of the covenant. The covenant has now been repealed. And I ask you whether they could so act today? A. I think that gets into this question of—I think they could not—if the covenant is a legally enforceable matter—•••

Q. I take it you are assuming that if such actions were attempted, the plaintiffs here would ask [Judge] Gelman to enjoin the Port Authority from doing that under the covenant? [276] A. Yes, I'm fully familiar with all the legal—
T 253-25 to 276-2.

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Q. You will see that Mr. Landis asked, "Now, let us assume at this point in time, a 100 million dollar bond issue, the purposing being to finance an investment of the Port Authority in mass transit that would not be self-supporting and a sale of a competitive bidding, what is your opinion as to what those bids would be," and that you thought that the issue would be more costly. T 276-10 to 276-17.

Excerpts from Testimony of John F. Thompson

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[277] The Witness: Yes, yes. I think the situation you hypotheticate there would be in the market the equivalent of the situation in which the Port Authority announced today on a 100 million dollar issue two weeks from now for whatever purpose, and this is a question that I have reviewed with our market people to considerable effect, and the general opinion that I get is that in this market it would cost the [278] Port Authority an interest cost of some 8½ percent. The quotations currently on outstanding Port Authority bonds indicate yields, interest rates to the investor of something like 6.50, 6.80. This indicates to me that such an issue coming to market would immediately drop the secondary market for all other Port issues. And we calculated it by some 6 to 10 points. T 277-17 to 278-11.

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[279] The Court: And Mr. Sovern has said, as I understand in giving the answer which you ultimately did, did you assume that the bondholders were in court challenging the validity of the repeal of the covenant?

Mr. Landis: I don't see any point in asking him if he assumed something that we all know is true.

The Court: Well, let him answer.

The Witness: I understood the question states what is your opinion as to what those bids would be. That assumes that the sale of the issue would go forward to the date of receiving bids without [280] court action. The question of court action did not enter my mind in answering that question.

Mr. Sovern: Now, your Honor, Mr. Landis has just said we are all assuming the court action.

Excerpts from Testimony of John F. Thompson

The Court: No, no, no, the witness has said—you asked him—

Mr. Sovern: Yes.

The Court: You asked him specifically whether he assumed when he gave his answer that there was a bondholder action challenging the validity of repeal.

And he said he did not.

Mr. Sovern: He did not assume that.

The Witness: No.

Mr. Landis: So your Honor, that is not my understanding of his question. What he said is he did not assume a decision.

The Witness: I did not —

The Court: All right. He did not assume a decision.

The Witness: I did not assume [281] either way. I assumed that I was asked where such an issue would sell, what bids it would receive, and I tried to simply answer that question without that—at that time, we were talking markets and not covenant. T 279-12 to 281-6.

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[284] Q. The next sentence of that paragraph under consideration is, "The Board of Commissioners is committed to preserve the credit of the Port Authority which is vital to the present and any future undertaking of the agency." Do you agree with that statement? A. I certainly agree with it as what would be their statement of preference. That obviously is what they would say, and this was one of the things I was responding to in my reply to Commissioner Ronan.

Q. Do you agree with the final sentence of the paragraph?

Excerpts from Testimony of John F. Thompson

The Court: I thought that was the final sentence.

Mr. Landis: It is.

Mr. Sovern: No, the final sentence is, "Governor Byrne—"

The Witness: Governor Byrne—I wasn't there. I don't recall seeing his statement. I presume he said that. This is what I would say if I were in his place doing what he did.

Q. Would you regard it as conciliatory? [285] A. Oh, it's in a sense, yes, but I would also regard it as saying, "We're taking a drastic action here, but hold still, it won't really hurt."

Q. How does that differ from what Governor Rockefeller did? A. I think Governor Rockefeller spelled out the possibility of compromise on the issue much more fully. T 284-1 to 285-9.

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[287] Q. Now, it is suggested in the brief of Counsel for the Plaintiff that one of the virtues of the covenant is that it would prevent the States from foisting a white elephant upon the Port Authority—that is to say, that if no bonds were issued, the Section 7 and 1.3 tests would not come into play and that therefore there is a risk that they just might make a gift here, and I don't attribute all the details of it, but in your opinion, if the covenant's repeal is upheld, do you understand that the States would then be free to avoid the protections of the 1.3 tests and the Section 7 certification by simply giving the Port Authority some deficit generating facility? T 287-5 to 287-16.

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[288] The Witness: I think there is a very real possibility of this. It is again, a legal question in considerable part.

Excerpts from Testimony of John F. Thompson

Q. And so that is one of the safeguards afforded in your opinion by the covenant that is not otherwise vouchsafed to the bondholders? A. I would think those circumstances would—

Q. Are you familiar with Section 7 of the Resolution establishing each of the series of bonds? A. Yes, I think we went over that yesterday. T 288-15 to 288-24.

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[293] Q. May the General Reserve Fund be used to pay the operating expenses for a facility for which bonds have not been issued? A. No, the General Reserve Fund may be used to pay for all operating expenses for a facility on which bonds—

Q. May the Consolidated Bond Reserve Fund be used to pay the operating expenses of a facility for which bonds have not been issued? A. I would think not, no.

The Court: You have answered the question.

Q. Now, you also testified yesterday that you regard the Section 6 covenant, the mass transit covenant as more exact, I believe, that was your phrase, but if it was [294] not, please correct me, than the 1.3 [and] Section 7 reassurances.

Is that your testimony? A. Yes, I used the word "precise" rather than exact, I think. I guess they are synonyms.

Q. At that time, the Court asked you about the definition of self-supporting. Do you recall that? A. Yes, you are now referring to the Section 6 covenant.

[295] Q. And you regard that as a precise definition? A. Precise in the sense that it must be referring solely to the expectations of this one facility.

Q. As you read that, could the states of New York and New Jersey agree that they would give all of their mass

transit enterprises to the Port Authority with a pledge of tax support for those facilities for the ensuing ten years and then get the necessary certification that the facility was self-supporting? A. There is other language in here that deals, I believe, with recurring debt from some other sources. T 293-12 to 295-14.

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[296] Q. You do not see anything in this covenant that would prevent the kind of public action [297] that I have indicated in my question earlier? A. Which the states would pick up for ten years and then run?

Q. And then Whammo. That's right. They don't say what they will do.

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The Court: They don't say.

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Q. They simply make a ten-year commitment. A. It looks as though it might technically comply.

Q. Why do you say technically comply? It would be possible, would it not, as far as you can tell? A. As far as I can tell at the moment. I would want to study the matter a good deal further before giving an informed opinion on it.

Q. If that is a permissible reading of the covenant, is that a subject for bondholder concern? A. The situation is very hypothetical. It would require all the bodies to be in on the deal, as it were. I think it is too hypothetical for me to pass judgment on it at this point.

The Court: Have you ever given any consideration to that possibility?

[298] The Witness: No. I think that whatever consideration has been given to that possibility has been on the basis of the states would act in a matter like that in good faith; having started it, it is very hard to stop a subsidy once you have started it.

Q. The basic assurance here is that the states and the Authority would behave in a responsible way. A. No, the basic assurance is that it would be for ten years self-supporting.

Q. And the bondholders are not concerned with the eleventh year? A. I think that gets into a sort of never-never land. It is pretty theoretical. I would not want to answer that, yes or no.

Q. I think I must press you, Mr. Thompson. As I read the covenant, it seems to me to permit exactly what I have suggested to you. You do not read it contrary. You have testified that you give a great deal of advice based on the covenant, and I ask you whether that advice is based on the assumption that this is not going to happen and that it is not going to happen because the basic [299] premise of bondholder reliance is that neither the states nor the Port Authority are going to engage in suicidal pacts and are going to conduct their affairs in a way that will enable them to continue as a viable entity. A. Which means in this case that they would have put their name on the line for a pledge of revenues, the estimates of revenues and debt service to satisfy the self-supporting requirements.

Q. I am assuming that those estimates are impeccable, not only in the sense that everybody behaved with honor at the point at which he made them out, but that unlike all other estimates they prove to be accurate and that the states did indeed keep that as a self-supporting facility for the entire decade. No one has made any promises for the eleventh year. It would not be dishonorable by any measure of good faith, would it, to refuse to renew a commit-

Excerpts from Testimony of John F. Thompson

ment when you made no commitment that you would renew the commitment? A. I did not understand you to say that the states made a commitment limited to ten years.

The Court: That was the assumption.

The Witness: They made a commitment to do it is what I understood you to [300] say.

Q. For ten years and no longer. A. Then I think you would have some trouble in the market.

Q. You think that would cause the Port Authority to have difficulty marketing its bonds now or in the eleventh year? T 296-24 to 300-8.

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[304] The Court: Make that assumption, that both states [305] have adopted a referendum which enables the Legislature to pledge for a ten-year period their revenues to pay the deficits. All right?

The Witness: Yes.

The Court: Now go on with your question.

Q. Would anyone who bought bonds with such a covenant in them—and by such a covenant, I mean the 1962 covenant—be relying on the covenant or on other protections for his security? A. The question assumes that someone would buy bonds. And if they were ten-year bonds, somebody would.

Q. I ask you to assume that they are Port Authority bonds marketed in the period between 1962 and 1973 is the last—1973. The 1962 covenant was in the 20th and to the 39th series. You have testified at great length and in great detail about relying on that covenant. You may have observed that we think that perhaps people relied on something else.

Excerpts from Testimony of John F. Thompson

And I am asking you now whether if that covenant permits that kind of behavior people were relying on that covenant or the other protections [306] which include the integrity of the operation both of the Port Authority itself and of the governments of the two states. A. I simply do not think that the Port Authority would go along with the projection of such a situation or that the states would do such a foolish thing as to vote a commitment for a half or a third of the life of a bond if they were doing something. You know, covenants and laws operate in a real world and deal with real situations; and this is not one.

Q. You are not concerned about the states of New York and New Jersey dumping their mass transit on the Port Authority? A. Now you are asking me a different question. I am not concerned about the hypothetical situation that you raised.

Q. What aspect of my hypothetical situation do you regard as unreal—academic, as you prefer to call them? A. I regard the notion that any responsible person in the Governor's offices or the Legislatures or the Port Authority staff or Commissioners would put together a device involving a ten-year covenant of support or something in order to sell 30-year bonds.

[307] Q. If that were the only way that you could both finance mass transit, as you put it, to meet the problems of energy and urban matters, if that were the only way or adjudged to be the best way to meet the problems with mass transit, why wouldn't they do it? What is there magical about a ten-year commitment or a thirty-year commitment if there is nothing wrong with it? A. I would like you to go sometime through the procedure of assessing a bond issue and looking down the road where the revenue comes from. Your Honor, this is just so unreal that it is silly. T 304-25 to 307-13.

Excerpts from Testimony of John F. Thompson

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Q. Isn't the reason that you are not concerned about this possibility that you have confidence [that] the states and the Port Authority, all 3 [308] as you noted, will not get together to adopt a plan that would obviously destroy the fiscal integrity of the Port Authority? A. I certainly think they won't get together to do anything as foolish as you have suggested, if that answers your question. T 307-23 to 308-6.

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[309] Q. I'd like to come back to the covenant for just a brief while longer.

Mr. Thompson, in stating that you relied on the protections afforded by the 1962 covenant did you rely on the pledge that neither the States nor the Port Authority will use any of the Port Authority's revenues for mass transit except insofar as the facility is self-supporting or its deficits fall in conjunction with those of the Hudson and Manhattan within the 1/10th of the General Reserve Fund limitation? Did you rely on that? A. Yes, certainly.

Q. Did you rely on anything else in the covenant? A. In the covenant?

The Court: Within the covenant?

Mr. Sovern: Yes.

Q. Was there anything else of importance in the covenant to you?

The Court: I assume when you say "covenant" you mean the legislation in 1962.

Mr. Sovern: To be precise Subsection B. As I say I'm excluding now for purposes of [310] simplification the first part which is not [in] issue. A. Subsection A has not been repealed.

Excerpts from Testimony of John F. Thompson

Q. Exactly. A. I think that summarizes the covenant, what we relied on.

Q. Yes. I'd like to come back to something else we talked about a while ago. Did I understand you to testify earlier this morning that if the Port Authority were given a white elephant that all of the revenues of the Port Authority operation, operating revenue would be pooled in order to support that before debt service would be paid? A. That's the way I understand it. It's under the net revenues that are placed the debt. T 309-4 to 310-13.

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[312] The Court: If no Consolidated Bond has ever been issued for the establishment, acquisition, effectuation, construction, rehabilitation or improvement of a white elephant, can the deficits of the white elephant be a charge upon the net revenue of these facilities that are enumerated in the preceding paragraph prior to the payment of the debt service rquirement and all the rest?

Mr. Sovern: Thank you, yuor Honor.

The Witness: I don't see anything here which prevents it. This is a pledge of revenues to Consolidated Bonds. It tells where Consolidated Bonds get their revenues. It doesn't say how the Port Authority shall operate its projects or keep its accounts otherwise.

Now, I think you said yesterday that [313] Newark Airport is operating at a deficit. Its about the only operating expenses there come from the other airports.

Q. So one of the reasons for your believing that the Section 6 covenant is important is that you believe that the

pledged revenues of all of the other Port facilities may be diverted to carry their losses even before that debt service requirements are met? A. No, sir, I do not believe that the pledged revenues may be diverted because the pledged revenues are net revenues.

[314] Q. All right. Thank you.

You believe then that in determining the net revenues of the Port Authority for the purposes of the Consolidated Bond resolution, that the Port Authority is entitled to pool both facilities for which Consolidated Bonds had been issued and other facilities for which no bonds had been issued? A. So far as I know, their accounting and their method of operating pools their revenues from all their facilities and there must be some for which Consolidated Bonds were not issued.

Q. I gather that it is because you believe that such pooling is possible that you regard the covenant as an especially important protection? T 312-10 to 314-13.

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[315] A. No, I won't have those words put in my mouth. I believe that this is one situation that might arise that makes the covenant important.

Q. Thank you.

At page 14 of Plaintiff's trial brief, it is said and I quote, "While Plaintiff concedes that in rare instances a State's contract can be constitutionally abrogated by a proper exercise of the State's never abdicated police powers," and it goes on, what I want to ask you is whether you are aware of the proposition contained in the language which I just read to you? T 315-2 to 315-12.

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The Witness: Your Honor, a day or two ago, I read a brief prepared by someone on this subject

which cited some cases pro and con and came to the conclusion that this case was in the class of those where the police power would not [316] prevail.

The Court: That is not the question which he asked you.

The Witness: I am aware.

The Court: You are aware?

The Witness: I am aware that there have been these cases and a number have been adjudicated.

Q. When did you first become aware of them? A. I think in a general way I have been aware of that sort of thing since graduate school days, probably. T 315-21 to 316-10.

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[317] Q. Did you know anything about inter-State compacts, the need for Congressional consent thereto? A. Since a suit was raised in this regard, I have become aware of this contention. I think I testified yesterday that it was not a contention which I took seriously, namely that any covenant must be approved by Congress because [318] there have been a number of past covenants, and I cited one yesterday, regarding the distance within which the States would not build any competing bridge and to my knowledge, that was not approved by Congress, nor was it considered necessary, and looking at it in the practical way, that, your Honor has suggested I do, this seemed to support the validity and the enforceability of the covenant that we are here concerned with.

Q. So your testimony is that you first learned that there might even be an issue as to the need for Congressional consent for the '62 covenant sometime after the Plaintiff instituted this action against the State of New Jersey? A. No, this other suit that the young man was here on.

Excerpts from Testimony of John F. Thompson

The Court: He means the *Gaby* case.

Q. The *Gaby* case? A. And its predecessor in New York State.

The Court: There was a prior New York litigation.

Mr. Sovern: The State will now mark for identification a story from the Daily Bond Buyer, Monday, June 24, 1974. It will be S-7. It came from the files, here is a copy for the witness.

I call your attention to column two. The second full paragraph.

[319] Did you see this story at the time it was published?

A. Yes.

Q. And you noticed that the Daily Bond Buyer says, "Repudiations of Solemn Pledges are Not Unique."

Do you agree with that? A. Well, I think it is in relation to what follows.

The Court: No, he is asking you whether you agree with that statement, not what the writer intended.

The Witness: Well, there have been other repudiations of solemn pledges granted. Some of them have been taken to Court and beaten down too.

Q. All right. A. This article, by the way, is a sort of editorial that John Winders does every week. To say that this is what the Bond Buyer says is not quite descriptive of the type of thing it is.

Q. Would you give the witness P-11, please?

P-11 is Moody Bond Survey, June 11, 1974.

Excerpts from Testimony of John F. Thompson

I call your attention to the final paragraph in column one.

In particular, the second sentence, "Both States have the right to alter corporate charter rights under constitutional provisions enacted following the famous case [320] of the *Trustees of Dartmouth College against Woodward.*"

Did you see that assertation when it was published? A. Yes, and I did not fully-understand it.

The Court: I concur. T 317-20 to 320-4.

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[322] Q. Mr. Thompson, does the institution of a lawsuit affect the value of a bond? A. Under what circumstances?

Q. Have you ever bought any bonds that were involved in a law suit? A. Where the validity of the bonds was involved in a lawsuit.

Q. I will start with that. A. If it was a new issue, my good friends in the bond legal firms would give an opinion on it, so I would not [323] be confronted with the question.

Q. And I am not referring to this case now. Have you ever been in a situation where you had to make a decision as to whether to participate in an offering or advise a client to purchase bonds that were involved in litigation in any way? A. This is a matter of such varied degree—

The Court: He is saying any form of litigation, for openers.

The Witness: We were involved not too long ago in an attempt to revive part of an issue down in Texas where there was some litigation started about the ownership of the property to be taken over for a generating plant.

Relying on the attorneys in Texas, we felt that the litigation was really part of the bargaining process over the price of the land, did not involve the

validity of the bonds and we were willing to try to proceed. We were unsuccessful because our partners did not go along.

I know that is not a whole answer to your question, but your question covers so many different possible situations. T 322-16 to 323-23.

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[325] Mr. Sovern: I'd like to ask the witness next about P-11. Will you give him a copy, please?

The Court: Yes. P-11. You already referred to that.

Mr. Sovern: I am referring to a different entry now, your Honor, the same paragraph, however.

By Mr. Sovern:

Q. At this time the final sentence at the end of column one, what is suggested is a considerable period of uncertainty and, perhaps, time lies ahead of these matters are litigated.

Uncertainty is not the bondholder's friend. Do you agree with that? A. Yes, certainly.

Q. And would that apply to this case? A. I think that's what he's talking about, isn't it?

Q. And you agree with the assertion with respect to this case? A. That a long period of uncertainty lies ahead, yes.

Q. And that it is not a bondholder's friend? [326] A. Uncertainty is not a bondholder's friend.

Q. And would presumably affect—strike presumably. And would affect the price of the bonds in the secondary market? A. Yes, it would affect them somewhat. T 325-1 to 326-5.

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By Mr. Sovern:

Q. I would like next to call the witness's attention to P-10, news release, Securities Industry Association, dated 5/15/74? A. Yes.

Q. I call your attention to the final sentence of the release. You think bond prices are affected by assertions that say "measures such as the proposed repeal are destructive of investor confidence and thus of public credit; the most certain [327] effect is to impair the ability to finance future public projects"? A. What is your question about it?

The Court: Do you agree with that statement? It is the last—

Mr. Sovern: Well, I am sorry.

Q. It is, do you think that statement would affect the price of Port bonds?

The Court: Oh.

A. Well, this statement was, I believe, one of several dealing with the Governor of New York when some of us were attempting to affect his decision.

The Court: That doesn't answer his question.

The Witness: I don't think it had any market impact, your Honor.

Q. Because it was a private document given only to the Governor? A. It may well have been published somewhere.

Q. Look at the top of the page on the left-hand side, it says "news release" on one-half of the page and on the other side its says, "for immediate release." It was a press

release, wasn't it? A. I don't remember that it was very widely [328] published, but it was a press release. You are quite right.

Q. Very good. Now that you know it was a press release, do you think it affected the price of the bonds? A. No, no, because what it says in that last sentence was the obvious to any investor.

Q. I'd like the witness to look next at P-12, that is, an article from Barron's dated 6/3/74. Do you have that article before you, Mr. Thompson? A. May I speak off the record.

(Discussion off the record.)

Q. Do you recognize that article? A. Yes, I think so.

Q. Did you have anything to do with its preparation? A. I think Miss or Mrs. Pacey came in for an interview about it at one time. I've forgotten whether she agreed not to quote me directly, or, perhaps you know. You read it more recently.

Q. I have a very bad copy. As nearly as I can tell she did not quote you. But how would you describe the circumstances of her interviewing you? [329] A. Well, she called up and said she wanted to do an article on this subject and someone had given her my name as somebody who might inform her on some of the considerations involved. At that time I was able to grant her an interview.

Q. Do you think this article had any effect on the price of Port bonds? A. The date isn't indicated and I have forgotten.

Q. This is the way it was produced for us. Oh, it's June 3, 1974? A. I wouldn't have thought of it as something having any effect on the market, no.

Q. Nothing in it would give bondholders concern? A. Well, it mentions the repeal of the covenant, but that was

covered in other news items that people already knew. I don't think this was the first information they had about repeal of the covenant. T 326-17 to 329-20.

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[330] Q. There is nothing else in that article that would be troublesome to bondholders? A. Well, the overall question it raises is about moral obligations certainly would confirm something that's troublesome to bondholders, yes. T 330-3 to 330-7.

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[331] Mr. Sovern: S-9 is a *New York Times* story headed, "Port Authority Abandons Mass Transit Opposition." T 331-2 to 331-4.

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Mr. Sovern: There is no dateline on that story, your Honor, but from its content it plainly was on May 1, the day following repeal in New Jersey and the holding of a press conference. T 331-11 to 331-15.

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[332] Q. I call your attention to the bottom of the column where it is said that the: United States Trust Company contended that repealing the covenant would jeopardize the agency's—meaning the Port Authority—the agency's financial capacity to back its bonds and impair its credit rating for future issues.

Do you think that would affect the price of bonds? A. That the United States Trust Company suit said that, no.

Q. I did not ask you that the United States Trust Company suit said that. I asked if the fact that they said this would affect the price of the bonds. A. No. I think they were just stating a truism in the investment world.

Excerpts from Testimony of John F. Thompson

Q. You think a public announcement by the largest holder of Port Authority bonds whose decision to dump on the market, you said, to dump any large number of bonds, you said would drive prices way down—the announcement by that largest holder and the trustee both, that the agency's financial capacity was being jeopardized and its credit was being impaired would affect the price of the bonds? T 332-4 to 332-24.

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[333] The Court: Would the making of the statement itself and its being reported in the press as reflected in S-9 affect the price of the bonds in your judgment?

A. Not considering the fact that the event had already been fully reported, the event of repeal.

Q. So that the price was as low as it was going to go? A. I am not going to try to predict what the price would be that day or that week. T 333-7 to 333-15.

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Q. You say that the Trust Company's assertions about the impaired capacity of the Port Authority had no effect on the price of Port bonds in the secondary market, because people already knew about the repeal of the covenant? A. Yes.

Q. Is that your testimony? A. Yes, I will go with that.

Q. And so the assertions of assessments [334] of a security by its largest holder do not affect the secondary marketprice of that security? A. Not when they are statements of things that are generally and fully recognized in the investment community.

Q. Have you ever bought a bond about which it was said—a bond or any other security about which it was said

Excerpts from Testimony of John F. Thompson

that its financial capacity was jeopardized and its credit rating impaired?

The court: By whom?

Mr. Sovern: By the largest holder of that security.

The Court: If it was, you know—

Q. If the largest holder of the security made those assertions would you go out and buy the bond? A. It would depend entirely on my own independent judgment of the situation.

Q. Have you ever used your independent judgment to buy such a bond? A. I have used my independent judgment to buy bonds when others thought that there were difficulties and would not do so, yes. T 333-18 to 334-21.

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[335] Q. Yesterday you testified about the Port Authority's facilities and the breaking of a common thread with the acquisition of the H & M. How was that common thread broken? A. The facilities acquired or constructed up to then had all been expected eventually to become self-supporting. H & M was not.

Q. Self-supporting at what point in the future? [336] A. Within a reasonable time, within three, four, or five years.

Q. Were those expectations fulfilled, to your knowledge? A. In what cases?

Q. I am asking you about your understanding about the Port Authority's experience with deficit facilities. Do you know of any cases in which their expectations were not fulfilled that the enterprise would become profitable within a reasonable period of time. I think you said three or four years. T 335-17 to 336-11.

Excerpts from Testimony of John F. Thompson

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A. I am not sure that my facility knowledge of the Port operation is sufficient to give you a full and accurate answer. I have understood that one or two facilities from [337] time to time have not done as well as hoped, but on the whole the reverse is true. T 336-23 to 337-2.

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Q. So your assumption that the Port Authority's moving from what had been almost entirely, with one or two exceptions, profitable enterprises to mass transit was a major factor in your concern about the acquisition of the Hudson and Manhattan? A. Yes, it was a factor of concern.

Q. And it continues to be a major concern down to today. That is to say, if the repeal of the covenant is upheld you are concerned that that pattern of profit making activity will be broken with the introduction of this deficit generating facility. A. I understand that is the purpose of the repeal.

Q. So the answer to my question is yes. A. That is a concern, yes.

Q. Now yesterday you gave as an example of the political pressures that are brought to bear on governors and the reason for bond holder fear, the fact that the governors vetoed the PATH fare increase. Is that correct? A. Yes. I understand that I mis-stated the exact procedure that took effect from lack of knowledge, that [338] actually the governors had already signed the minutes of the appropriate meeting when the fare request was approved, but that later on they persuaded the Commissioners to withdraw the application to the Interstate Commerce Commission for permission to raise the fare.

Q. Now, I believe it is accurate to say that you have throughout your time on the witness stand referred to the

Excerpts from Testimony of John F. Thompson

covenant as a bar to engagement of the Port Authority in mass transit. Is that correct? A. In deficit producing mass transit.

Q. Does it permit the Port Authority to operate bus lines that run at a deficit? A. The covenant, I believe, has the word rail in it. So bus lines are not included.

Q. Did most investors know that? A. I have not taken a poll. I don't believe I know the answer to that. T 337-6 to 338-17.

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[339] Q. Are you familiar with the economics of the operations of the airport part of the Port Authority's business? T 339-6 to 339-8.

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[340] Q. Are you familiar with it? A. I have not reviewed with the Port Authority a breakdown of their operation into airport and other things. I don't know the figures.

Q. Do you know whether the airports have been doing better or worse than they used to do? By used to, to take a time period, three years ago. A. I don't know. On the one hand there has been a lot of capital improvement at Newark. On the other hand there has been the effect of recession here on air traffic.

Q. So you don't know. A. I don't know.

Q. Do you know about the impact of energy developments on the traffic patterns at the bridges and tunnels? A. I received some overall information on that a year ago when the energy crisis was at its height; and it seems to me that for a time there was a decline of something like ten percent. But this taxes my memory as far as being exact is concerned.

Excerpts from Testimony of John F. Thompson

Q. But your recollection is there has been some deterioration in the revenues from the auto traffic? A. There was during that period. I think, and I am not sure I can cite a source for this, but I think it has pretty much come back to where it was. T 340-1 to 340-25.

[351] By Mr. Landis:

Q. In discussions that led off with regard to a credit report issued in January of 1962 with regard to the 19th series of consolidated bonds of the Port Authority, Mr. Sovern asked you and it is at page 211, line 10, Mr. Sovern asked you, "Did the 19th series contain a covenant?"

And you responded, "No, because the covenant had not yet been passed by the two Legislatures."

Is it also true that there was no legislative power to take over the Hudson & Manhattan at that time? A. That is true, the legislation authorizing the takeover of the Hudson-Manhattan had also not been passed.

Q. I show you a copy of the Port of New York Authority official statement in connection with the issuance of the 19th series, the date of the official statement being December 22, 1961, and I ask you to read the last paragraph of the discussion on page 13 of that document, the discussion being entitled, "Hudson & Manhattan Railroad Acquisition and Improvements Study."

I ask you to read the last [352] paragraph. T 351-1 to 352-2.

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[354] The Witness: The paragraph reads, "The Port Authority has no present effective legislative power which would enable it to undertake the financing and implementation of this proposal."

Excerpts from Testimony of John F. Thompson

The status of the pending legislation on the subject is reported in the next subdivision.

Mr. Landis: Thank you, Mr. Thompson, we have previously had reference to the official statement that is contained in the stipulation, that official statement being the statement for the 41st series, which is the last series of bonds which had been commissioned by the Port Authority, a copy of which you have in front of you.

Would you refer to page 17 of that document and would you specifically [355] refer to the language that starts, "It is presently intended. . ." Just below the center of the page, and review that language over to the break in the middle of the next page.

A. I have read it.

Q. Do you recall having read that at the time that official statement was circulated? A. Yes, I did, sir.

Q. And in making recommendations with regard to the purchase of that series, did you rely on those statements? A. Yes, sir. T 354-8 to 355-13.

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The Court: Mr. Thompson, have you ever read a document which is exhibit 5 annexed to the stipulation of facts in this case which was a speech made by Mr. [356] Daniel Goldberg, the then general solicitor of the Port Authority, in October, 1964.

The Witness: Yes, I read it recently.

The Court: Do you recall having read it at the time or approximately at the time it was published in April of 1964.

The Witness: I don't recall specifically reading that at the time, sir. It was one of a series of

lectures to a section of personnel of the Port Authority and I am not sure it was distributed to some of the rest of us at the time.

The Court: Do you recall ever having conversations with Mr. Goldberg concerning the financial structure of the Port Authority in its economic prospects and the state of the bonds and the consolidated bond resolution?

The Witness: Your Honor, I am quite sure that I have had. I have known Mr. Goldberg for many years and I have had conversations with him on a number of related subjects and I am sure this must [357] have come into it.

The Court: Because during the course of this talk, he does make reference to the concerns of the financial community, and I am sure you would be included in that group.

In the reading of this document which you say you did recently, did you take note of some of the statements that he made to the effect—and his speech was given prior to the adoption of the covenant—that in fact under the existing statures and consolidated bond resolutions, there were no monies available within the Port Authority financial structure to finance any deficit rail transit operations.

The Witness: I remember that he made such statements, yes.

Q. Is that your understanding of what the effect of the statutes and consolidated bond resolution would be without the covenant?

The Witness: Would have been then or—

The Court: Now, irrespective of the covenant, is it

your understanding [358] at the present time that under the statutes which were in effect and are still in effect and the terms of the consolidated bond resolution pursuant to which these bonds were issued, that there are no monies available within the Port Authority structure which could be used for mass transit that are not already pledged to existing bondholders?

The Witness: I am not sure that without the covenant some of the money in the bottom line would not be so useable, your Honor.

[359] The Court: When you say the bottom line, what is it?

The Witness: The consolidated bond reserves.

The Court: That would be the only possible source of monies then for the use, or to cover deficits resulting from mass transit operations, which the Port Authority might undertake?

The Witness: Well, your Honor, that would depend on how the project was integrated into the Port Authority. As I said yesterday, I have seen no specific proposals from advocates of repeal [as] to just what their intention is. And I have heard many comments about sums like 100 million dollars a year and so on that give rise to fears that they are looking at something much further up the scale.

Then I don't feel at all confident to answer what would in effect take place.

The Court: Now, I call your attention to page 23 in this same exhibit in which Mr. Goldberg discusses—T 355-22 to 359-25. * * * [360] his interpretation and the effect of the Section 7 certification which you had indicated was a subjective test which

was not adequate to safeguard the interests of the bondholders. I would ask you to read it, because I am sure you would not recall the whole paragraph.

The Witness: No, I am reading it.

Yes, I have read it, sir.

The Court: Mr. Goldberg seems to view this Section 7 certification as being a very rigorous and precise one, and he ends up with the statement that this Section 7 certification has "helped to allay the fears of the financial communities."

I gather from the testimony which you gave us yesterday, particularly that [361] interpretation of Section 7, and also that you disagree with his conclusion that the financial community's fears were assuaged by the conclusion of this certification requirement.

The Witness: Yes, I think implicit in his statement at that time was the record of the Port Commissioners from the whole Authority up to that time of complete independence from political discussions. And I think that is implicit in what he says here. And since then there have been changes in that respect. Mr. Goldberg goes on later, as you know. In order to further allay the fears of the financial community he is forecasting the 1962 covenant.

The Court: He is advocating some form of covenant at the conclusion of his talk. That is certainly so.

The Witness: It pretty much outlines what the 1962 covenant became.

The Court: Now in order to perhaps help me in my understanding of what the financial structure of

the [362] Authority's bonds are, if you take a look at the bottom of page 21, and continuing over on 22, right to the bottom of 22—

The Witness: Right.

The Court: I have read this I don't know how many times. But at the conclusion Mr. Goldberg says that in point of fact the Authority would not be in a position under its then financial structure to be given a deficit operation and be called upon to pay the operating deficit and any debt service requirements which it might entail, because all of the moneys, all revenues, are the Authority's and were pledged for existing facilities or to outstanding bond issues.

The Witness: I think that is the substance of what he is arguing.

The Court: Do you agree with that?

The Witness: I agree that the pledges that he describes are accurately described. I do not believe that the situation through the Section 7 certification that he describes was sufficient to [363] satisfy the investment community that these things would not take place.

The Court: Now I am not concerned with the Section 7 certification. But what I want to know is whether you agree with what he seems to be saying here, that the Authority's revenues are already pledged pursuant to the statutes or the consolidated bond resolution so that it could not pay or would have no monies left to pay for any deficit operation that might be handed to it, by the action of the States.

The Witness: I think first he indicates that they will not take the money outside the Port Authority.

Then he goes on to document the fear that a group of deficit ridden railroads might be taken over, and that is what he reads into the Section 7 certification. The last paragraph on page 22 documents an additional fear that this might be done within the Port Authority. And then he goes on to speak of the Section 7 certification.

[364] The Court: Would you agree with his statement in that paragraph in the middle of page 22, that the Authority's revenues could not be used to subsidize the private railroads to the extent of their commuter operating deficits—estimates they were called in 1961?

The Witness: As matters then stood, I think that was probably correct, yes, sir.

The Court: Now if you could turn to that series 41 official statement—T 360-7 to 364-13.

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The Court: Page 62, where Mr. Sovern was asking you to read, and following up some questions which he had; again, I just want to find out what your interpretation of this representation is in the official statement.

As I read this, could the states give to the Authority, let's say the Delaware & Lackawanna and the Susquehanna [365] and the Erie Railroad for nothing, having acquired them by whatever means they did; and could revenues of the Authority which are pledged as described here then be used to pay any deficit resulting from such rail operations?

The Witness: Your Honor, I have reread this section since my testimony of that this morning, and I have to say that I am simply uncertain on it and

do not know what the legal outcome of such a controversy would be.

The Court: I am trying to isolate it. Assuming that they could not use any of these pledged revenues for such purposes, then the consolidated bondholders would really have nothing to fear, would they?

Because all of the revenues from all of these facilities as described there are pledged to the consolidated bonds.

And if you got down to Section 5 it is to pay the debt service on the consolidated bonds, and the balance is pledged as security for the consolidated [366] bonds, to be paid into the consolidated bond reserve fund, except such amounts as must be paid to the general reserves.

The Witness: Yes.

The Court: So assuming that the interpretation I think that Mr. Sovern was contending for this morning is correct, then none of the revenues of the Port Authority from any of the facilities which are mentioned in Section 4-i, could ever be used to finance a deficit transit operation, and that would be pursuant to the terms of the consolidated bond resolution.

The Witness: Your Honor, I am not certain that follows.

The Court: I realize you have some question in your mind. I have a question mark. We hope that it will be cleared up.

The Witness: If it does follow, I have no idea of why the effort was made to repeal the covenant. T 364-18 to 366-23.

[367] The Court: Again reading the same paragraph, and if you will make that same assumption,

the only way that revenues from any of the Port Authority's existing facilities could be used to finance the mass transit operation would be if the Port Authority were able to issue a consolidated bond to either purchase or rehabilitate or improve that facility. Is that right?

The Witness: That would be a way to do it, yes.

The Court: Now really doesn't the financial community have control over that situation?

I mean, the financial community has a lot of concerns and fears and so forth for the integrity of the covenants and for the security it has for its bondholders. But doesn't the financial community and its ability to reject the [368] offering of any bond by the Port Authority have ultimate control whether the Port Authority or the states can ever engage in this kind of mass transit operation?

The Witness: Your Honor, implicit in your question is a concept of the financial community as a much more unified thing than it is. There are many competing firms that do things on a variety of bases.

There are firms who would not hold out, as you say, if they could get a 9½ percent bond to sell on the basis of this, they could very well try to do it. This would be quite contrary to the interests of other bondholders who had gone before them. I think that is the difficulty. The financial community is not a unified organization. T 367-5 to 368-19.

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[369] Mr. Landis: Your Honor, may I have one question.

By Mr. Landis:

Q. Assume, if you will, Mr. Thompson, Consolidated Bonds that the Judge referred to only need be one $1,000 bond sold to anyone, the proceeds of which would purchase from the State of New Jersey all the deficit generating commuter railroads in New Jersey that are now privately owned, those railroads having been previously purchased for their market value by the State of New Jersey. T 369-2 to 369-11.

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[370] The Court: Given your experience with the integrity of the Port Authority Commissioners and the manner in which they have conducted themselves over the last what, fifty odd years, would you consider that to be a realistic fear, that the Port Authority [371] would issue a $1,000 bond of a consolidated —pursuant to a Consolidated Bond Resolution to bring into the pie the mass transit deficit operation? Do you think that they would ever do such a thing?

The Witness: Your Honor, ten years ago I would have answered certainly not. Today if you asked me about the Port Authority staff I would say certainly not.

We have noted from time to time that the Commissioners are under greater and greater political pressure in these matters. I cannot give you as strong an answer now as I would have before.

The Court: Would you say it would be unlikely?

The Witness: Your Honor, there has been so much going on in this thing that seemed unlikely to me from the start and unintelligent, the things that have been promoted in this field that it's somewhat unlikely. T 370-21 to 371-19

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Excerpts from Testimony of John F. Thompson

Recross-Examination by Mr. Sovern:

Q. So one of the fears the covenant protects against is the issuance of a $1,000 bond and the taking in of all the deficits. Is that correct? A. That is a hypothetical question which technically [372] I think fits into the provisions and would work.

Q. You say it would be somewhat unlikely that such a step would be taken, and, therefore, I take it, you believe that there is some risk that it will be taken. This morning you regarded as absolutely unthinkable that the States might make an arrangement with the Port Authority for a ten year support arrangement. Do you still regard that as absolutely unlikely, or is that somewhat unlikely? A. Now, this was a ten year voted covenant?

The Court: Right.

A. (Continuing) Yes, I still regard that as very unlikely because it doesn't fit together.

Q. That's more unlikely than that they would issue a $1,000 bond for the assumption of all the mass transit facilties in the metropolitan area. Is that correct? A. I think we might not attach too much weight to the $1,000. T 371-21 to 372-17.

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[382] (Exhibit S-21, Official Statement, 19th Series, was admitted in evidence.) Q. This was the official statement for the 19th Series, was it not, Mr. Thompson? A. Yes, so I understand.

Q. And you testified earlier on your cross-examination, the 19th Series was sold [with] no special charges for fears

Excerpts from Testimony of John F. Thompson

of special mass transit. Is that correct? A. I believe that's correct. T 382-8 to 382-16.

The Court: Could I ask you one question? Has Moody's changed its rating of Port Authority bonds since back in 1971 or so?

The Witness: No.

The Court: It is still A today?

The Witness: Still A today.

The Court: Has Standard & Poor's [383] changed its rating of the Port Authority bonds since 1971?

The Witness: I believe not, your Honor. T 382-19 to 383-3.

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Excerpts from Testimony of Lester Murphy, Jr.

LESTER V. MURPHY, JR., James Lane, Lloyd Harbor, Long Island, New York, sworn.

Direct Examination by Mr. Landis:

Q. Mr. Murphy, by whom are you employed and in what capacity? A. Barr Brothers & Company, 40 Wall Street, vice president of the firm responsible for trading positions in dollar bonds.

Q. What is your educational background, Mr. Murphy? A. Colgate University, 1949, graduated with a BA.

Q. How long have you worked in the municipal bond field? A. Twenty-five years.

Q. When did you begin your employment with Barr Brothers? A. October of 1950.

Q. And what is your present position with [384] Barr Brothers? A. I am a principal in the firm. We are now a corporation. I worked in the Trading Department. As I say, I am responsible for the dollar positions and also cover institutional accounts.

Q. When was Barr Brothers incorporated? A. 1971.

Q. And what was your capacity prior to that? A. Prior to that, we were a partnership. I was in partnership in the firm from, I believe, it was 1959; basically involved in the same capacity as I am now.

Q. And you are presently a stockholder in the firm? A. Yes, I am.

Q. Is it privately-held? A. Yes.

Q. And prior to reaching the position of partner in 1959, what were your duties and areas of responsibility? A. I started as a trainee, in 1950, started from there; became a junior trader and then into institutional sales.

Q. And since 1961, what have been your responsibilities, your duties and areas of responsibility? A. Again, in the field of responsibility in the trading position of the firm.

Excerpts from Testimony of Lester Murphy, Jr.

[385] Q. What are your day-to-day activities in that posture? A. Well, I sit at a training desk that is a long table with a lot of direct wires to banks, other major stock exchange firms, municipal bond dealers and maintain markets in several hundred issues of municipal bonds, much like a specialist might be on the New York Stock Exchange.

Q. What are the areas of business that Barr Brothers does? A. We are involved in underwriting municipal bonds and dealing in municipal bonds in a secondary market.

Q. Do I understand your testimony to be that you are involved in the dealing operation, the secondary market dealing operation? A. I maintain an active market in roughly two hundred issues, yes.

Q. What is the size of the firm? A. Total employees, we are relatively small, about 35 employees, we have slightly in excess of two million capital, principally amongst four principal stockholders.

Q. How old is the firm? A. Over fifty years old.

Q. How would you characterize the status of the firm in the municipal bond trading in the secondary market? T 383-8 to 385-25.

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[386] A. We maintain, I'd say, daily trading positions that range anywhere from five to eighteen million. I'd say that our current inventory positions have been running around twelve or thirteen million bonds.

Q. Are you a large or a small trader, how would you characterize it? A. I'd say in the secondary market, big traders.

Q. How big compared to the other traders? A. I'd say in the field of dollar bonds, I regard ourselves as probably in the top three as for dollar volume business.

Excerpts from Testimony of Lester Murphy, Jr.

Q. Who are the other two? A. Salomon Brothers and Weeden.

Q. Are they competitors of yours? A. Very highly competitive.

Q. Describe the clientele of Barr Brothers? A. Well, our clientele, as I say, I sit at a trading desk and probably speak to or handle two hundred phone calls a day and the type of people I would talk to would be banks, [387] trust companies, other major municipal bond dealers as well as large stock exchange firms.

Q. I believe you said that Barr Brothers is considered the dealer in the business? A. Correct.

Q. Do you deal with brokers in the business? A. Well, to give you an insight as to what a dealer is, we maintain markets and we deal with our own capital and if we position bonds, it is for our own accounts. We attempt to buy bonds naturally at a spread whereby we can make a profit, very much like somebody that is in a used car lot, who is standing there and looking at cars coming in, willing to make a bid, hopefully, to sell them at a profit.

We are standing in a marketplace every day maintaining active markets, providing a function of making markets and hopefully intend to make a profit on the spread. T 386-7 to 387-16.

[390] Q. Do you deal in bonds of the Port Authority of New York and New Jersey? A. Yes, we do.

Q. Is your clientele in this regard local or national? A. National.

Q. Do you specialize in particular bonds?

Does the firm specialize in certain bonds? [391] A. We tried—we have developed a reputation of being very active in what we call the dollar bond market, which encompasses most of your toll roads, power authority type facilities,

Excerpts from Testimony of Lester Murphy, Jr.

Port facilities, bonds of that nature which were issued in term form and are traded in dollars as opposed to being traded on a yield basis.

Q. When you say you make a market, what does that term mean? A. A market would entail offering to the caller the bid side of the market and the offered side of the market and the size which is of very important consideration in making the market; not that the quote is in 85 bid offered at 86, how big is that market?

Q. In other words, you mean the size of the commitment you are willing to make when you make the market? A. Size of the market is part of the market. Very often you might have a market that is 85-6, but it is only good for $25,000. Whereas in other securities it might be good for a million dollars. So size is as important a consideration in the market.

Q. How long has Barr Brothers been dealing in Port Authority bonds making the [392] market? A. I would say since the late '40's.

Q. How much trading volume has Barr Brothers done in the course of the day's trading in Port bonds in the secondary market over the last three years? A. I would say that our daily turnover in volume is approximately a total of about two-and-a-half million. And I would say that our Ports turnover can range anywhere from 100,000 in a day to one million and a half. But I would say on an average it is probably more like in the neighborhood of ten percent of our total turnover.

The Court: Which would be what?

The Witness: On say two-and-a-half million dollar turnover—

The Court: $250,000?

The Witness: Yes, $250,000, but depending upon the activity of the market in certain issues.

I mean, we might trade two million Ports in one day. It is a fluctuating situation.

Q. Does your firm deal in Port Authority bonds in greater volume than others? [393] A. I could not answer that. I sort of pride ourselves as being one of the three most active firms in that field.

Mr. Landis: I offer the witness as an expert here.

The Court: Are there any questions on qualifications?

Mr. Sovern: No. T 390-17 to 393-8.

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[394] By Mr. Landis:

Q. Mr. Murphy, you, of course, are aware that this litigation involves the repeal of the 1962 covenant of the Port Authority that controls the Port Authority, are you not? A. Yes, I am.

Q. What is your general understanding of what that 1962 covenant involves? A. My general understanding it limited the scope of mass transit for the Port Authority.

Q. Are you familiar with the covenant in any greater detail than you just described? A. The covenant?

Q. The 1962 covenant. A. No, nothing more than that.

Q. In your business are you in any way involved in the analysis of municipal bonds? A. Well, as I said before, we are making positions for our own account in a greater number of issues and we try to keep abreast of the current financial positions of all the issues that we deal in.

Q. Meaning the trading situation? A. Well, we keep—we receive naturally [395] earnings statements from the

toll roads, the power facilities and other agencies in whose securities that we trade. So we try to keep abreast of the financial situation in everything that we deal in. If there is a situation that appears that it's faltering financially naturally we want to be aware of this.

Q. In 1973 did Barr Brothers own any Port Authority bonds? A. Yes, we did.

Q. You own any now? A. Yes, we do.

Q. What effect did the repeal of the 1962 covenant that took place early in 1974 have on Barr Brothers' attitude toward the Port Authority bonds?

The Court: June of 1974, be more precise, the repeal became effective.

Q. (Continuing) Well, the process that became effective in June of 1974. A. Well, as I recall we were hopeful at the time that Governor Wilson would veto that, because we felt that if the covenant was repealed we felt it would have a very poor effect on the [396] market and we have always maintained the positions both long and short in Port issues, but when Governor Wilson signed that he signed it with, as I understand, remember reading in the press, with a fair amount of reluctance and hoped that the decision could be finally settled in the courts.

With the idea in mind that the Port Authority would become more involved in mass transit we were extremely cautious about our positions, and I'd say adopted a much more conservative trading attitude as far as our positions in Port bonds.

Q. What do you mean by "extremely cautious" and more conservative trading attitude? A. Well, on the initial signing by Governor Wilson or right after the signing of this repeal we noticed that there was a number of Port bonds

that seemed to be offered for sale in the market, and in appraising our markets every day and looking to whom buys and sells the securities, we felt that the market trend was down, and we tended to take a very cautious position as far as how many bonds we were long and tried to play the market on what I would say was the short side.

Q. Would you explain that, the short side? [397] A. A short sale is selling a security that you don't own, hope to cover it back at a profit. In other words, in maintaining a market if a market was 85-86 and if we could make a sale at 85½ without owning the bonds we would make that sale with the hope that the market would decline and cover that bond back in at a profit.

Q. Does the term "spread" have some relationship to your operation? A. Well, spread refers to profit margin. I would say that we wanted more spread, more profit margin than any commitments that we took in Ports, because the market was subject to a fair amount of selling in Port bonds.

Q. Why did the repeal of the covenant change Barr Brother's attitude towards Port bonds? T 394-1 to 397-17.

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[398] The Witness: Well, I would say that with the repeal of the covenant it was paramount in most people's minds that deal in these securities that there was a breach in the contract, and we felt that with a breach in the contract that, first of all, it was something I don't think I've experienced since I've been in the business, and secondly, we felt that the spread in the Port Authority operations into greater mass transit would have a very poor effect on the performance of their bonds, and that other institutions indicated that to us, and that, therefore, we adopted

a position of much more conservative, much more conservative attitude towards our long positions.

[399] Q. You spoke of investors. What effect did the repeal have on the attitude of investors towards Port bonds? A. Well, part of their function in the marketplace is to try to track certain relationships of various dollar bonds. We don't do any professional analysis or advice in the form of investment counselling. We merely provide markets and spread relationships, and we have found that for many years that you could, when certain spreads develop, that you could talk a customer into selling a bond and buying, let's say Ports, but we found that subsequent to this repeal of the covenant, that most of the major institutions that we did business with, and I wouldn't say most, I don't know of any that would then buy Port Authority bonds. They crossed it off their list.

Q. Did you have any direct communication with those institutions? A. Yes. T 398-9 to 399-20.

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[401] By Mr. Landis:

Q. And the investors that you communicated with, without identifying what they said to you, what was the nature of the communications?

The Court: What was the subject matter?

Q. (Continuing) The subject matter. A. Well, as I said we attempt to provide a service to institutions whereby we are calling markets, showing spread relationships.

We found that institutionally Port Authorities were no longer an acceptable exchange in that the investor, institutional-type of investor, sophisticated type investor would

not any longer buy Port Authorities. If he was to sell a Kansas Turnpike or Indiana Turnpike wheretofore he would [402] buy Ports when a certain spread relationship developed, he no longer would buy Ports.

Q. Without trying to name every one, which institutions do you refer to, what are the names of them? A. The names of the accounts?

Q. Yes. A. Well, I'd say Fireman's Fund, which is a large insurance company in San Francisco, major banks in Chicago, the First National Bank of Chicago, major banks in New York City, Bankers Trust Company, First National City Bank, insurance companies, the Connecticut General, the Hartford Fire Group and others.

[403] By Mr. Landis:

Q. And those have been customers over the years as to Port bonds? A. That's correct.

Q. You indicated in your testimony that there would be exchanges, you gave some examples. Do those have a name, those exchanged, trades? A. Swaps.

Q. Exactly what does that entail and what are the reasons for it also? A. Well, to try to be simple, if that investor was able to sell, say, a million par value bonds at 80 and buy a very similar bond quality-wise intrinsically at 75, he might very often make the trade because from the proceeds from the sale, he is able to buy more bonds and therefore increase his income and in the case of the Ports, the spreads had widened to, in some of the trades, I recall, to 15 points or more but it was no longer a question of spread relationships. It was a turndown of the security based on how good the investor thought the intrinsic value of the Port bond had become after the repeal.

Q. In other words, despite the increased spread, you could not interest people in [404] taking back Port bonds? A. Correct.

Q. Do you have an example of that, could you give an example? A. The names I had cited that had normally been [buyers of] Port Authority bonds, no longer would consider them as a fair, acceptable return.

Now, Bankers Trust had a large swap in November of last year and they would not take anything, they wouldn't take any Ports back. Anybody who sold Ports that we did with major trust companies for tax swapping purposes, did not buy Ports back. They were willing to sell the bonds, but they were not willing to buy them back.

Q. You previously referred to the impact of the repeal on the price of the Port Authority bonds. Would you explain that in more detail? A. Well, the repeal, as I say, changed not only our attitude but changed the institutions' attitude about whether or not they were willing to own this bond with the threat of the Authority becoming involved in mass transit.

Now, most institutional investors and most people in our business, historically, know that [405] mass transit financing of which there have not been that many, but the ones that I am familiar with, most of them got in serious trouble.

Bi-State, which is a joint agency between Illinois and Missouri sold a bond for the purposes of mass transit. Those bonds are presently in default. Chicago Transit Authority had severe difficulties with their debt and I found that the word "mass transit" or "transit facility bonds" is one that literally shows deficits and widening spread, so that the quality of the bond, I find, is unacceptable institutionally.

Excerpts from Testimony of Lester Murphy, Jr.

Q. During this time of price decline that you referred to, what other factors were at work? A. Well, as I said before, I said that one of the factors was that it was a change in the investor's attitude on what he believed was a contract between the states and that he felt that if they could do this with this bond and become involved with mass transit, even though it might have to involve a certain coverage test, it was a politically dangerous position because, as we all know, the subway fares, etcetera, are more or less sacrosanct and I think anyone who is familiar with or following [406] the MTA, has recognized that they are in deep financial problems. Also, I think that a major change in the thinking was that the last experience we had along this line was the Triborough Bridge & Tunnel Authority which hoped to alleviate some of the MTA's financial burdens and they went to the bondholders, obtained a two-thirds vote of the bondholders, offered the bondholders a quarter of one-percent over the existing interest rates on the outstanding bonds and closed the lien so that the MTA would then be able to get the surplus over a 120 coverage so that this was a radical departure, I'd say, from the previous type changes that I have seen made in bond indentures.

[407] Q. You referred to the size of the market in bonds since repeal. Could you explain in detail what you meant? A. The size of the market I would say immediately after the repeal was quite active. I would say that there was substantial selling of Port Authority bonds. As time went on it became increasingly heavier, particularly at the end of the year, because a number of institutions and fiduciaries availed themselves of the opportunity of selling Port bonds to establish tax losses. But the market had been extremely thin. Most dealers were not willing to position much in the way of Port bonds because of the outlook of the Port entering the mass transit field.

Excerpts from Testimony of Lester Murphy, Jr.

Q. Let me direct your attention specifically, to the Port bond issues commonly called the 6's of 06 and 08. Are you familiar with those? A. Yes I am.

Q. In fact those are issues that have their final maturity, the maturity in the years 2006 and 2008 and issues with a coupon at 6 percent. Is that correct? A. That is correct.

Q. Can you take the period now from the time of repeal where you had testified to the condition of the market since that time, take the period from then until December 1974; can you characterize the activity of the [408] prices that were bid for those bonds? A. I would say that in general—

> Mr. Sovern: Exactly what dates do you have in mind?
>
> Mr. Landis: From the period roughly of June 1974 to December 1974.

A. I would say that the market in general of Port bonds experienced a rather severe decline. T 401-10 to 408-8.

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Q. Could you characterize the change in price, if any, of the bids for those bonds in the period from December 1974 until today? A. The bonds have had a very, very substantial recovery. I would say that from the middle of December until the present time has been a 20 point recovery in the bonds.

Q. Compared to the general activity of the market during this time, could you characterize the decline and the rise that you have just described? [409] A. I would say that the decline was naturally greater during the period from June through December than the rest of the market. The turn arounds from the first of the year to the present time has been substantially better than the rest of the market.

Excerpts from Testimony of Lester Murphy, Jr.

Q. Can you explain the variations? A. Well, as I have stated before, most dealers, like ourselves adopted a cautious long position. However, most dealers fearful of the tax selling in the bond particularly adopted a position where they were short the bonds. The markets were quite thin. But most dealers like ourselves had rather large short positions in these bonds.

Now, coupled with the lack of selling when tax selling ended at the end of year, coupled with the Federal Reserve's position on money, their posture of easier money, what happened was that dealers who were short these bonds scrambled to try to cover their short position.

So what you had there was a technical situation in the market where a number of dealers were short Ports. Tax selling subsided at the end of December. The bond market took on a strong tone.

Q. You say the bond market, do you refer to the bond market in Ports or generally? A. Generally.

But this accentuated the upward movement of Ports, [410] because I think that people who own Ports now are willing to await the outcome of this case recognizing it was rather imminent.

I think the people who decided to sell sold many months ago. The rest of them are gambling that the Courts will find in their favor. And I have not seen any supply of bonds come into the market. We as dealers cover short positions. It cost us in excess of ten points. T 408-17 to 410-8.

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Q. Would you characterize the upswing that you just described in prices since December 1974 of the Port 6's of 08 and 06? A. Characterize the upswing?

Q. Yes.

The Court: He has.

Excerpts from Testimony of Lester Murphy, Jr.

A. It was a thin market. There was a change in Federal Reserve's posture on money and dealers short covering, a technical situation.

Q. Could you give it a name? A. As an example, I think this might be important, the most dramatic movements on the up side have been in the more second grade quality paper. Jersey Sports which was [411] 7½ percent bonds that had been selling in December at 65 and recovered to 80 today. Urban Development Corporation—New York State Urban Development Corporation, a bond that is under a cloud that had substantial recovery again for the technical reasons I cited about the Ports. So your poorer quality, less regarded tax exempts, that had the slowest recovery because of a technical situation.

Q. Is there a name that describes this adjustment that happened in the prices? A. Is there a name?

Q. Yes. A. I just characterized it as short term technical situation.

Q. Which is what your testimony has been; in other words there is no other magic name.

Has the repeal had any effect on the attitude of investors with regard to other bonds other than the Port Authority? A. Certainly, the number of institutions whom I have cited feel that if a covenant was to be repealed, a so-called contract with the issuing states, the concern now becomes increasingly more acute for bonds that are so-called moral obligation bonds.

In the case of moral obligation bonds the [412] problem is whether the legislatures will appropriate the needed funds to keep them in business. So, I think that the overall position that I have found from the people as a market maker that I talk to from day to day to day is one of increasing greater concern about how good the contract is that they

are buying, and I think will lead to much higher interest rates.

Q. Did the effect go even beyond the moral obligation bonds? A. Yes. There was an issue of Power Authority bonds that sold within the last two weeks a $150 million issue that normally would have much greater national acceptance than it did. The acceptance was hurt.

Q. Did your firm participate in the underwriting of that bond? A. Yes, we did.

> The Court: When you say Power Authority, do you mean the New York State Power Authority?
>
> The Witness: Yes, New York State Power Authority.

Q. I show you exhibits that have been marked P-94 and P-95. You are familiar with these are you not? [413] A. Yes I am.

Q. You have seen these before. Yes.

Q. Were the bond issues shown on those documents chosen at your suggestion? A. Were these chosen at my suggestion?

Q. Were they placed there at your suggestion? Was that your thought to create that? A. This particular chart?

Q. Yes. A. Yes sir.

Q. It refers to Kansas and Indiana Turnpike bonds, does it not? A. Yes, that is correct.

Q. Could you describe those issues? A. They are toll road facilities dependent upon the net revenues of the facility to service debt. Traffic naturally would determine the toll revenue income.

Q. Did the issues have similar characteristics to the issues of the Port Authority of New York and New Jersey that are shown on the same P-94?

A. The bonds have similar coupons, similar maturities, similar average life, dependent upon toll revenues—I think they have great similarity.

A number of trade swaps have been done in the past between Port issues in Kansas and Indiana; it has been a very common trade in the past. In a tracking relationship, as you can see here, there is quite a bulge that develops subsequent to the repeal.

Q. Would you consider upon the basis of the knowledge you have expressed and upon the illustration of the movement of bid prices from January 1974 to June 1974, that the issues shown on P-94 are comparable? A. They appear to track pretty closely, yes. T 410-13 to 414-16.

[415] Mr. Laulicht. • • • I would like some voir dire on these documents before they're introduced. T 415-11 to 415-14.

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[417] Mr. Laulicht: Now, you testified, Mr. Murphy, that in January of 1974, you would have regarded Kansas Turnpike issues as roughly comparable to these Port Authority issues. May I ask you whether the Kansas Turnpike, did it run a passenger railroad?

The Witness: Not to my knowledge.

Mr. Laulicht: To your knowledge, did the Port Authority run a passenger railroad on January, 1974?

The Witness: Did the Port Authority?

Mr. Laulicht: Yes.

The Witness: Yes.

Mr. Laulicht: Was that a deficit producing operation?

The Witness: It is. I don't know if it was known at that time.

Mr. Laulicht: You are not sure [418] whether in January, 1974, PATH operated at a deficit?

The Witness: They did, but I can't tell you what it was.

Mr. Laulicht: To your knowledge, did the Indiana toll road run a passenger rail deficit facility in January, 1974?

The Witness: No.

Mr. Laulicht: Did the—either the Kansas Turnpike or Indiana toll road operate a World Trade Center in January, 1974?

Mr. Landis: We will stipulate the whole series of questions Mr. Laulicht is asking.

The Court: How do you know?

Mr. Landis: I suspect that they did not have three airports, they probably did not have tunnels under interstate rivers.

The Court: What is your point?

Mr. Laulicht: My final question was this: Doesn't the fact that the Port Authority runs a World Trade Center and I take it you're familiar with the problems [419] of the World Trade Center, it runs a deficit railroad and it ran that in January of 1974,

doesn't that tend to make these two issues not comparable?

The Witness: Well, first of all, the Port Authority shows that net revenue, I don't know how you take down their revenues, but they show net revenues on a comparable earnings basis for the facilities. I would consider them comparable.

Mr. Laulicht: I don't understand what you mean "a comparable percentage of revenue." Do you mean to show—

The Witness: The point is if the Port Authority shows 20 million dollars in net revenues this year, I am unable to break down how much is lost in the World Trade Center and how much is made in the airport facilities. I regard the net revenue, the bottom line as a consideration.

Mr. Laulicht: Irrespective of the type of operation that is involved?

The Witness: I would say—

Mr. Laulicht: As long as the [420] bottom line is satisfactory, you feel that is the way to judge a bond. Is that correct?

The Witness: As long as the bottom line, as the bond was presently constituted, yes. I would have considered them equal bonds at that time. T 417-6 to 420-8.

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[421] The Court: Irrespective of the spread that may have existed between [them, they], would be comparable in terms of investment quality and in the demand by institutions for these bonds or their willingness to purchase these bonds.

The Witness: I would say yes.

Excerpts from Testimony of Lester Murphy, Jr.

The Court: And didn't you also testify something to the effect that you arranged swaps by institutions for these bonds or their willingness to purchase these bonds.

The Witness: I would say yes.

The Court: And didn't you also testify something to the effect that you could arrange swaps between these bonds with your institutional clients because they were roughly comparable in the minds of the buyers?

The Witness: That's right.

The Court: That is enough to qualify the exhibits. T 421-2 to 421-23.

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[422] *Direct Examination by Mr. Landis Continued:*

Q. How would you characterize the relationship that is shown on P-94 to have existed between the bid prices on June, 1974, through January of 1975? A. It shows a much greater spread. It appears sometime in June that the bonds no longer tracked. T 422-5 to 422-11.

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[424] The Court: See, they both seem to track roughly on this chart right even into July, don't they? And indeed while the spread may have been widening there through the end of July they're still tracking.

Now, you get the real significant difference in the spread once you get into August where they are really diverging. Now, my question to you, Mr. Murphy is this: Do you know of any external factors affecting the Kansas Turnpike and Indiana Toll bonds between, say, mid-August and mid-November

Excerpts from Testimony of Lester Murphy, Jr.

of 1974, which would have accounted for their increasing in prices?

The Witness: Well, there were—

The Court: Were there any developments on there?

The Witness: You mean as far as [425] changes in their indenture or something to that effect?

The Court: Whatever.

The Witness: Well, the only thing that I can add to it—there was nothing in the way of a change in the bond. The only thing that probably created a greater upswing in those markets was that there was some debt retirement that occurred during that period. The debt retirement that occurred during that period, however, in looking back on it, they were always able to buy bonds on debt retirement under the market. In other words, if a sinking fund was to retire five hundred bonds in a month and the quote was let's say 70-72, it appeared that the sinking fund would be able to buy the bonds under the market. We were in an overall declining market, and a number of institutions were liquidating Kansas and Indiana's, but you did have a sinking fund operation that occurred in that period in that they did buy bonds for retirement.

The Court: All right. So that you are saying that that was one factor that might [426] have caused an increase in those bonds. Right?

The Witness: Yes. But the—

The Court: All right.

By Mr. Landis:

Q. Are you speaking, Mr. Murphy, as to the specifically sharp rise from August to November 1974, in those bonds?

Excerpts from Testimony of Lester Murphy, Jr.

A. I believe roughly that's what the Judge was making reference to, yes.

The Court: Yes, that's what I was making reference to.

Q. Now, characterizing the general trend from June or, perhaps, May of 1974 to the end of, almost the end of January, 1975, let me ask you to repeat your characterization of the general trend. I believe you previously characterized it, but just to lay a foundation for my next question, let me ask you to characterize that general trend.
A. During what period?
Q. From May or June, if you will, of 1974 through January of 1975?

Mr. Sovern: The end of January?
Mr. Landis: The end of the chart. A. Characterize the market for Port bonds?

[427] Q. No, characterize the difference, if any, in the trends of the Turnpike bonds as opposed to the Port Authority bonds all as illustrated on the chart. A. Well, I think the chart speaks for itself, that you had a widening of the tracking. It got extremely broad, I guess, in the months of September and October, and towards the end of December and January you still had a considerably wider tracking, let's say, than historically was the case.

Q. Do you have an opinion as to what external factor caused that wider tracking between the bid prices of the issues? A. I think I testified to that, that we have found that the Port Authority bonds were no longer acceptable on tax swaps. T 424-8 to 427-16.

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Excerpts from Testimony of Lester Murphy, Jr.

[433] [By Mr. Laulicht.] Q. You gave us several reasons why you thought the repeal of the covenant had had an adverse effect, and if I may summarize them, I believe you said that it was the fact that a contract was breached, and to your knowledge that had never happened before, that the increase in Port Authority involvement in mass transportation was not regarded favorably, and then you made some reference to what some other institutions told you and we, I think managed to keep [434] that out of the record. Which of those three would you rate as the most important?

The Court: Most important in relation to what? Let's define that.

Q. (Continuing) In terms of the adverse effect that the repeal of the covenant had?

The Court: On the secondary market?
Mr. Laulicht: Yes, on the secondary market.

A. It would be very hard to break down. When you break a contract down how an institutional investor would weigh that in terms of comparing it with getting the Port Authority involved in mass transit, I know both of them are red herrings. I know that when you mention "rapid transit" or "mass transit" to an institution it's entirely unacceptable, because it's demonstrated that the transit systems throughout this country are largely operating at deficits, and the institutional and professional investor is greatly concerned with security today. He doesn't want to buy something that's possibly going to cost him a lot of money.

Q. Well, why did any investor buy a Port Authority bond since 1962 if he didn't want to [435] get involved with something that had to do with mass transportation, and if

it's such a bad word? A. Well, I don't think that the history of the Port Authority has been revolving around mass transit. It's been a well-run, well-organized, well-managed Authority. It's continually shown good revenues.

Q. Is the fear then that by the repeal of the covenant the Port Authority now is going to be suddenly completely enwrapped in mass transit? A. No, I think that the fears, I think I've previously testified to, is that it's a—it's an abrogation of an agreement, it's a contract. It's as if I went and bought a car from General Motors and had a twelve month warranty, and all of a sudden they announced that it's only good for six months. I don't think that I'd buy another General Motors car. And I think this is the feeling in the investment community.

Q. Now, you testified, Mr. Murphy that one of the reasons for the increase in the price of Kansas Turnpike bonds and Indiana toll road bonds as reflected on P-94 was the fact that there was some sinking fund activity. Is that correct? A. Correct.

Q. Can you tell us how much of that [436] increase was attributable to that sinking fund activity? A. I think I can document that the purchasing that the sinking funds did was either at the market or below the market.

In a sense, if I could explain that, Judge, if you had a market that was quoted 70-72 and the trustee entered the market for an offering of 500 bonds he, quite frequently bought bonds at 69, indicating a number of institutions were selling the bonds, because they were too high, and these markets were basically small markets. It was one way that an institution can unload a lot of bonds.

Q. Institutions aren't unloading Port Authority bonds now, are they? A. No. To my knowledge, they're not, no.

Q. That means that the present price is not regarded by them as too high yet? A. My only feeling there would be,

I think, that they're hopeful that a decision would be such that they won't have to. T 433-18 to 436-20.

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[438] Q. Can you explain to me how it is that the price of Port Authority bonds appears to be in the low 50s in the July period, and it has gone up to 55 as I read this by the end of October. A. It was obviously a tracking in the market or an up tic there. These markets do not continue to go one way all the time.

Q. Didn't you tell me how demoralizing the market in Port Authority bonds was back through the end of the year? A. I characterized the market as having substantial selling immediately after Governor Wilson's signing the repeal. Subsequent to that, dealers like ourselves maintained a low profile as far as long positions. The markets were extremely thin. As [439] evidenced by what has happened in the last month, we have had a 20 point increase on very little supply. So when we talk about markets we're not only talking about quotations, we are talking about number of bonds traded, the size of the market which is more of a key factor than the quotes. T 438-11 to 439-6.

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Q. Isn't that what you are saying, that the bond prices don't matter very much if you don't know the [volume]? A. If you were in my business and you made that statement you would be out of business in a hurry. T 439-12 to 439-16.

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[443] Q. Let me ask you this: Assume that I show you that there are variations in the spread from week to week on P-95; do you feel anyone of them by themselves is significant or is going to tell us something? A. I think P-95 is merely a compilation of the numbers that appear in this

period. I think I testified that there was a wider divergence that has developed since the time of the repeal. I have also testified institutionally where we have made swaps with institutions out of Kansas and Indiana's into Ports is no longer an acceptable trade. T 443-3 to 443-14.

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[444] Q. As far as you are concerned, was the decision of the institutions not to buy Port Authority bonds anymore than their own investment decision, that is all that represents. Is that not correct? A. That's correct.

Q. As it turns out, assuming that that was the investment decision of the institution in December 1974, as it now looks, how would you characterize the wisdom of that investment decision? A. I would characterize the thinking as completely unchanged. I am unfamiliar with a major institution that would buy Port Authority bonds today.

[445] Q. That was really not my question. My question was wouldn't they have made money if they had another investment decision? A. Institutions don't usually buy and sell to make money. They buy for intrinsic value return. They don't buy and sell something out usually at a point or two profit over a week or two's time. They try to keep their money invested at all times.

Q. You talked about a 20 point profit since December, did you not, Mr. Murphy? A. No, I said—I said yes, there has been a substantial improvement in the price, correct.

Q. Doesn't the swap list concept constitute the playing of a point here and a point here, not twenty points, but a point here and point there? A. You are talking of a swap out of, let's say, Kansas or Indiana?

Q. Yes. A. A swap off of Kansas or Indiana—

Q. That is not my question. My question is you answered a prior question saying that institutions are not interested in a point here and a point there. If that is

true, why do they engage in these swaps you are talking about? [446] A. Let me explain that to you, sir. The swap would involve the sale usually of a fairly-large amount of bonds, let's say a million Kansas Turnpikes, at which point if the spread had tracked historically where you normally had a ten point spread and institutions could sell a million Kansas and then buy an issue that was done to a twenty point spread, it would be a very attractive swap, but once you have removed this Port Authority bond as an acceptable swap, the presentation of the spread means nothing.

We have presented these swaps and in a number of cases we are told by institutional accounts we won't buy anything in the New York or New Jersey area.

Q. In other words, Barr Brothers has recommended the purchase of the Port Authority bonds as a part of a swap, has it not? A. We have not recently because our history, as I explained back after the signing of the covenant was such that you don't call up a customer every day and say, "Would you mind buying Ports today," if he told you he won't touch the Ports.

Q. At some point you suggested a swap that would have involved the purchase of Port Authority bonds and from what you are telling us, is [447] even a 15 point difference was not enough to make the deal? A. Correct.

Q. But wasn't your bringing that swap to your customers' attention something that you thought would be to the benefit of your customers? A. We have not brought those types of trade to our customers, as I explained to you earlier. We no longer have accounts that buy Ports. T 444-13 to 447-9.

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[448] Q. Let me put it to you this way, would you recommend as part of a swap an investment security that you

Excerpts from Testimony of Lester Murphy, Jr.

considered a dog? A. Would I?

Q. Yes.

The Court: Depends on to whom.

Q. The Banker's Trust Company? A. That would be absurd, they have people who are doing research work, their own analytical staff. First of all, as I say, we don't do business, to speak of, with individuals. If we do one to ten percent of trade, we do trades with additional people who know what the hell they are buying and selling.

Q. Except they are gamblers, as you told us, they are professionals, but they are gamblers? T 448-9 to 448-25.

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[449] Q. Didn't you testify that the people who are now holding the Port Authority bonds and have had a 20 point increase are gambling as a result of this suit? A. No, my testimony was there has been a lack of institutional selling here. Hopeful that this decision will go in favor of the U.S. Trust Company.

Q. Did you use the word "gambling" in this connection, Mr. Murphy? A. Gambling on the outcome of the suit, possibly, I did. T 449-6 to 449-16.

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[450] Q. Let me show you some documents or some news stories fairly quickly.

S-1 is an article that appeared in the Wall Street Journal about the World Trade Center. T 450-21 to 450-24.

* * *

[451] Q. Were you aware of that story at the time, Mr. Murphy? A. That particular story? I cannot testify to that particular story. I have certainly been apprised that the World Trade Center is behind in some of its plans, yes.

Excerpts from Testimony of Lester Murphy, Jr.

Q. As far as you know, have those news stories, similar to what I just showed you in S-1 with respect to the World Trade Center had an adverse effect on the market price of Port Authority Bonds? A. Your question is whether these adverse stories on the World Trade Center, has it had any effect?

The Court: Adverse effect.

Q. Adverse effect on the bond price of the Port Authority in the secondary market? A. To a limited extent, it must have, yes. I can't think for every institutional investor, but I would say if it was I, I think it would.

The Court: Do you have any recollection of discussing the Port Authority problems with the World Trade Center with any of your institutional clients or [their] referring to any news stories in their conversations with you?

[452] The Witness: The only thing, Judge, that I can recall discussing was that the World Trade Center was experiencing some difficulty in renting space, but also that they anticipated to throw off $20 million to the revenues of the Port Authority.

Now, how they arrived at their costs, etc., I cannot answer those questions. T451-4 to 452-7

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Q. I would like you to pay some attention, if I may, to S-2. This is an article that appeared either on the front page of the Sunday Times or the front page of its financial section in November 1974, a very lengthy article as I am sure you will note. It is headed, "Port Authority has Fallen on Hard Times."

Do you remember reading this article a few months ago? A. I didn't particularly read it. I was familiar with it at

the time. [453] Q. How did you become familiar with it if you did not read it? A. In our office every day, we talk about this kind of news.

Q. What kind of discussions did you have in your office about this article? A. Well, just a general discussion as outlined here.

Q. Did you think that this article might have an adverse effect on secondary prices of Port Authority bonds? A. I don't know how to answer the question. I don't believe that that was discussed at the time because I think that—

> The Court: Based upon your experience trading in these bonds?
>
> The Witness: It might have some effect.
>
> The Court: It might?
>
> The Witness: Sure.

Q. If you look a little bit closer at the beginning of the articles, I don't want to take you through it, by any means. There are some very strong statements in this article. You have one New Jersey Commissioner saying "The Port Authority is dead in the water." T452-16 to 453-23.

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[454] A. I would answer that by referring to the chart, P-94, which would indicate to me that there was a more substantial drop during that period in Indiana's and Kansas than there was in Port Authority's, so obviously it did not have that much effect on the market.

Q. That is your opinion, Mr. Murphy? A. I am looking at the chart here. In the middle of November to the end of the year, it looked like the Indiana's and Kansas' suffered a much more severe drop.

Q. Do you know why they suffered their drop? A. There is a pat answer in our business. There are more sellers than buyers.

Q. Besides that pat answer, do you know why they suffered that drop? A. Besides that?

[455] Q. Yes, do you have any explanation for that drop? A. None, really, that I can think of, no.

Q. Now, if the article did not have that serious an effect, Mr. Murphy, can you tell me why on P-89 for the period of November we see the Port Authority dropping much, much further than the Massachusetts bonds did? That is P-89. T 454-11 to 455-8.

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A. Well, you are taking in a longer prospective there and I think I earlier testified there was substantial selling for Ports bonds in November and December. That is how we got ourselves in the bind on the short positions. T 455-12 to 455-15.

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Excerpts from Testimony of Michael Zarin

[466] [By Mr. Landis] Q. Mr. Zarin, I understand you are employed [467] by the Port Authority, is that correct? A. That's correct.

Q. In what capacity? A. I am Chief of the Finance Division of the Law Department of the Port Authority of New York and New Jersey.

Q. And you are, as I understand it, a member of the Bar? A. I am a member of the Bar of the State of New York.

Q. And you are educated as a lawyer? A. Yes, I am educated as a lawyer.

Q. And with a BA and LLB degree from what? A. I graduated from Dartmouth College with a degree of AB in 1953 and from Columbia Law School I have a JD degree, and graduated in 1956.

Q. How long have you been employed by the Port Authority? A. Since 1956.

Q. And in what capacities? A. I first started as a law assistant and almost immediately became an attorney, upon my admission to the Bar in 1956. And in 1965 I became Chief of what is now known as the Finance Division.

Q. Had you worked in connection with the [468] Finance Division prior to 1965? A. Yes. At that time it was essentially a Finance, Taxation, Insurance and Research Division.

Q. Was there some restructuring at that time? A. In 1965 two divisions were created out of the division that I have just mentioned, an Opinions and Appeals Division, and a Finance Division.

Q. Where were you employed before 1965, in what operation? A. Before 1965 I was a member of essentially the same division.

Q. You have had responsibilities in the area of finances of the Port Authority? A. Yes, I have.

Excerpts from Testimony of Michael Zarin

Q. Over the entire period of your employment? A. That is correct.

Q. And are you involved in any organizations in connection with your work outside the Port Authority? A. Yes. I have noted down the outside associations that I think has some bearing on these financial matters. Those include, I am a member of the Standing Committee on Debt Administration of the Municipal [469] Finance Officers Association of the United States and Canada. I am a member of the American Bar Association Local Government Law Section and its committee on liaison with the Securities Industries Association. I am a member of the Municipal Forum of New York. I am Chairman of the Law Committee of the International Bridge, Tunnel and Turnpike Association.

Q. Have you had any post law school education? A. I participated in and completed the Harvard Business School Advance Management Program in 1972. T 466-25 to 469-11.

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Q. Mr. Zarin, you are familiar with the subject matter of this litigation, are you not? [470] A. Yes, I am.

Q. Of course, as we previously established you are familiar with the circumstances under which you are called as a witness. Would you then please explain to the Court as you understand it, the meaning of the 1962 covenant and the relationship of the covenant to the other security provided by statute and contract to the consolidated bondholders of the Port Authority.

The Witness: Your Honor, before I do that, may I make clear something about my position here today?

The Court: Yes.

The Witness: And that really has a relationship to my position as an attorney for the Port Authority of New York and New Jersey. In that structure I make recommendations to the general counsel of the Port Authority, and he in turn recommends those things which he wishes to the Executive Director and to the Board of Commissioners.

So that not only in my discussion here today, but in practice as far as the Law Department of the Port Authority is concerned, my opinions and the statements are not binding [471] upon the Port Authority even in my work until general counsel has approved them.

And I just want to make clear, as I understand it, the Port Authority is not participating in the particular litigation between the United States Trust Company and the two States, and my appearance today is as a witness in that proceeding.

The Court: You are expressing your own opinions, really.

The Witness: Fine, thank you very much. I might say, of course, that the opinions even that general counsel expresses and gives to the Commissioners, the Commissioners themselves, as you know, being appointed from each State constitute the authority and make those decisions for the Authority subject to gubernatorial veto.

I think since the question is a very broad one I would like to step back just a little bit in time from the time of the covenant to the time when I became aware of the fact that the Port Authority was becoming involved in rail transportation and the efforts to become involved in rail transportation.

[472] The Court: Well, I am not particularly interested. I don't know whether counsel for the—

The Witness: I don't mean—

The Court: U.S. Trust Company may be, but I am not particularly interested in what the Port Authority may have done with respect to rail mass transit. All I am interested in is the structure of the bonds.

The Witness: That's right, and that is really what I—I don't mean to speak factually on that subject, just to make sure that the legal matter is on the table that we are discussing and the background of the legal matter is in order to become involved in this area. We had to so structure our legal and financial relationships to enable us to do so.

At first, it appears to be extremely difficult to get the deficit operation of any kind because the Port Authority initially was set up as a self-supporting agency, and as a bi-state agency, was one part of its structure.

[473] The other key part of its structure was the self-support structure, so when we were being called upon by the two states to go into passenger rail transportation, being a deficit area, we had to look at the structure again.

At first, we, all of the people who were looking at it, there was no way that we found initially. The first way that we found and developed was in connection with what is now the New York State commuter car railroad program, to which the two states passed legislation enabling each state to pick up the option of guaranteeing the commuter railroad car bonds which would be issued by the Port Authority

essentially as an agency outside the Port Authority's financial structure.

The Port Authority's experience in issuing bonds, entering its contracts, and building was to be utilized, but not the whole structure which we will talk about in a moment.

New York passed the legislation to that effect, adopted a Constitutional [474] amendment guaranteeing up to 100 million dollars of bonds.

Under that, the Port Authority has purchased and leased to various commuter railroads, including the Long Island Railroad, and what is now the Penn Central system in New York, hundreds of commuter railroad cars and that is a revolving 100 million dollars so that as principal has been paid off over the years, we have actually issued more than a hundred million dollars, but always as a limit of state guarantee.

The bonds are paid via rentals from the commuter railroads and if a rental payment does not come in, the State comes in to pay it. That has never occurred.

After that structure of participation, there was an additional call to the Port Authority to participate in commuter railroad systems and what was developed in order to permit Port Authority participation is the 1962 covenant.

The next step, as I remember the procedure, and I think that that being the next step, perhaps I ought to describe a [475] covenant as I understand it because I think before letting me give the background of how we arrived at that point.

In describing the covenant, I will try always to contrast the covenant or to compare the covenant

with all of the other protections and covenants under the statute and bond resolutions as I understand them.

The 1962 covenant is contained in Section 6 of Chapter 8 of the Laws of New Jersey, 1962, and the concurrent legislation which is Chapter 209 of the Laws of New York State of 1962.

In describing this covenant, your Honor, I think that I should at least initially confine myself to Section 6(b) which has been repealed, if that is agreeable to you.

That covenant is a very exact limitation on the deficit which may be incurred by the Port Authority in connection with passenger railroad facilities, in addition to those of the basic Hudson tube system which the Port Authority commenced operation in the latter part of 1962.

[476] The limitation is in two parts: One part would permit an additional deficit operation if the annual deficits, as measured in the statute, do not exceed ten percent of the General Reserve Fund of the Authority. That ten percent has an alternative computation, and that alternative computation is a computation of equity and amounts invested in facilities which is a one percent calculation, and the one percent calculation is really, as your Honor understands, analogous to ten percent of the General Reserve Fund, and the General Reserve Fund itself, being ten percent of the outstanding debt, ten percent of that amount is one percent.

However, being recognized that the debt of the Port Authority, of course, can be reduced, the General Reserve Fund being reduced, that permitted deficit would narrow. The alternatives would

measure, would be the amount which the Port Authority has invested in facilities which are paid up, so that you would have the ten percent of the General Reserve Fund plus the one percent [477] of the equity, the amount which has been paid, and the amount paid into the facilities by way of investment of Port Authority funds. These amounts are adjusted so that you essentially cannot bootstrap them by putting money into additional railroad facilities, increasing your debt, increasing the ten percent or in essence increasing the equity amounts.

Those are in broad outline the limitations, and I should point out that I believe you have in the record, the official statement in connection with the 41st series of bonds and the statutory covenant and really probably a more exact summary of it than the one I have been able to give you orally, the one which we have set forth on page 16 and 17 which actually appeared in the 39th series, official statement and all the other official statements.

[478] The Court: In order for me to just comprehend the effect of the covenant that gets us back to the General Reserve Fund.

The Witness: Fine. I intend to do that and I'll do that now.

The General Reserve Fund of the Port Authority is a Reserve Fund, Statutory Reserve Fund, set up under the General Reserve Fund Statutes of the Port Authority, which in its practical effect today states that the Port Authority shall maintain in the General Reserve Fund—and when I say shall maintain, that's to the extent that there are funds available to maintain a reserve equal to 10 percent of the outstanding bonded debt of the Authority.

It is really the debt which has been issued for terminal and transportation facilities and World Trade Center, of which that outstanding debt issued in the form of bonds for which the General Reserve Fund stands as a security.

10 percent of—the amounts of 10 percent of those bonds equal the present General Reserve Fund, and that is the fund against which this provision is measured that we have been [479] discussing.

The Court: Now, is there any other Statutory Reserve Funds the Port Authority is required to maintain other than the General Reserve?

The Witness: The General Reserve Fund and other statutes contain provisions under which the Authority may enter into agreements with bondholders, but I take it that those are not the agreements that you are talking about. You are talking about strictly statutory ones.

The Court: Statutory ones.

The Witness: And I don't recall that even the Consolidated Bond Reserve Fund is set up under statutory—under the statutes. I believe that that is set up under the Consolidated Bond Resolution.

So my testimony now would be and, of course, some of these questions that will come up are things that I may want to check, but my understanding is that this is the Statutory Fund, the General Reserve Fund is the Statutory Fund.

The Court: All right. Now, at the time the General Reserve Fund was authorized by legislation it was to consist of 10 percent of [480] the par value of all bonds issued by the Port Authority and currently outstanding. Is that your understanding of the General Reserve Fund?

Excerpts from Testimony of Michael Zarin

The Witness: That the intent—well, your Honor, that is the general understanding of it and I don't mean at all ever to quibble except I think I'm here as the person to give some really technical understanding to the extent I'm able.

People in our organization that frequently recall this requirement in conversation, and I'm always careful to point out when that occurs that it's a requirement only in the sense that it's specified in the statute.

If the General Reserve Fund were to fall below 10 percent that is not an occasion for bondholders, for example, to feel that a covenant has been breached.

The Court: No, I understand that.

The Witness: It's only to the extent that there are funds available that we would maintain it at 10 percent.

The Court: Right. The statute does not require you to have the 10 percent there if [481] you don't have it.

The Witness: You've stated it precisely.

The Court: So that's what the statute required as of 1931, and that applied not only to bonds then currently outstanding, but bonds thereafter issued.

The Witness: Bonds thereafter issued of the types stated there, bonds legal for investment and issued for particular terminal transportation purposes. I don't have the statute before me.

The Court: All right. Now, between 1931—well, before we get to that, the statute also authorizes the Port Authority to pledge the monies in the General Reserve Fund for the repayment of interest on bonds thereafter issued by the Authority. Is that correct?

Excerpts from Testimony of Michael Zarin

The Witness: Yes, your Honor.

The Court: Now, after 1931 the Port Authority did build certain facilities under the terms of what I have described in the papers here as the General Reserve Fund Statute?

The Witness: That is correct. T 469-24 to 481-23.

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[502] The Court: Is there anything which should be inserted in this chronological history before we get to the adoption of the consolidated bond resolution?

The Witness: Your Honor, the explanation and discussion which we have just had effectively demonstrates the closing, in my judgment, of all of those prior liens, so that we may, in essence, in our discussion, take all of the prior obligations of the Port Authority before 1952 and say that they really do not need to form part of our discussion because the liens on those bonds were closed by these trusts and the bonds, themselves, while at one time they were so-called "open end issues," in that more could be sold of them, that ability to sell more of those bonds was closed when the consolidated bonds came into being, so I think we do not need at least for the purposes of this discussion, as I understand it, to consider pre-1952-issued obligations.

The Court: And assuming that the Port Authority never issued a consolidated bond and that this is all that was outstanding and then actually all of the revenues coming in for the [503] operation of your facilities, for the maintenance charges, could be allocated to any purpose consistent with the charter of the Port Authority? In other words, none of

these bonds have any call on any revenues that come in?

The Witness: Those bonds, G & R, Air Terminal, Marine Terminal Bonds, are not presently part of the revenue flow.

The Court: Then you do not make any allocation of revenues to any of them aside from the payment of the operating expenses under the facilities themselves?

The Witness: As far as the obligations themselves are concerned, they are satisfied by payments by the Trust Company.

The Court: Does the Port Authority have any bonds outstanding prior to 1952 that were issued prior to 1952 which have any call on any revenues of the Port Authority at the present time?

The Witness: At the present moment, there is no call on any such revenues. I would say that the trust agreement itself provides that all of this is proper during the maintenance [504] of the trust. If we were not to maintain the trust for some reason and the trust was not to function, then it is conceivable that the revenue flows would still go to those bonds, because I think the agreement talks about upon the establishment then during the maintenance of the trust, we have defeased the liens. T 502-1 to 504-7.

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[510A] The Court: I guess we are ready for 1952, consolidated bond resolution.

Now, in the sequence in which they occur, I am not so sure whether I am exact in this, would you explain first the 1.3 test under the consolidated bond resolu-

tion? First of all, what does the consolidated bond resolution cover in terms of facilities?

The Witness: The consolidated bond resolution—

The Court: At the time it was adopted, what did it over, what did it authorize the Port Authority to do?

The Witness: Well, of course, any [511] resolution—

The Court: At the time it was adopted, what did it cover, what did it authorize the Port Authority to do?

The Witness: Well, of course, any amounts which were to be invested after 1952 through the issuance of the Port Authority obligations beginning with 1952 and extending for quite some period of time thereafter, were consolidated bonds. There were no longer any G & R, air terminal or marine terminal bonds issued, so the consolidated bonds were issued for all the facilities of the Authority from that point on, whether they be bridges and tunnels on which the G & R bonds may have a first lien or air terminal bonds and so forth.

Then the first facility immediately following, in other words, a new facility immediately following on that would have a first lien on consolidated bonds.

The Court: As I understand it from Mr. Goldberg's book, the consolidated bonds could be issued for any purpose whatsoever? T 510A-11 to 511-24.

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[512] The Witness: Yes, your Honor.

The Court: And in fact, historically, you did issue consolidated bonds for improvements to G&R facilities as well as air terminal facilities and marine terminal facilities?

The Witness: Your Honor, perhaps I should say, just so that my statement is clear, that Mr. Goldberg's sentence says, "After unlimited purposes," that is any purposes that the Port of New York Authority was authorized by statute to go forward with and to use the general reserve fund [513] in connection with.

Now, the general reserve fund, so that we cannot issue for anything but those things that we are authorized to.

The Court: Of course. The general reserve fund substantially applies to the consolidated bonds which were issued by the Port Authority?

The Witness: Yes, your Honor.

The Court: Okay. So these he goes on to say are open-end bonds. In other words, you could continue issuing bonds under the terms of this resolution for old facilities and further improvements and so forth.

The Witness: Yes, subject, of course, to the limitations which your Honor alluded to before.

The Court: Yes. Now, in order to issue a consolidated bond, the 1.3 test must have been satisfied, there must be, I assume, a certification that the 1.3 test will be met.

The Witness: The 1.3 test must be met prior to the issuance of a consolidated bond [514] issue.

The Court: Now, would you explain the 1.3 test?

The Witness: Your Honor, the 1.3 test under the consolidated bond resolution is contained in the consolidated bond resolution adopted on October 9, 1952, by the Port Authority of New York and New Jersey. At that time, the Port of New York Authority.

The Court: What page are you on?

The Witness: That resolution appears, beginning of page 55 of the official statement with respect to the 41st series. That is Exhibit 2.

The Court: What page then are you on?

The Witness: The consolidated bond resolution, Section 3, commences on page 57, the condition under which bonds have been issued [is] condition 3 appearing on page 59.

The Court: Condition 3.

Now, there are four conditions, any one of which must be met before you can issue a consolidated bond. Is that correct?

[515] The Witness: Yes.

The Court: Are you saying that the Authority has elected only to issue bonds under condition 3?

The Witness: I am saying, your Honor, that we would issue obligations—that is to say, assuming that there is a project for which Commissioners wish to issue obligations, we would then examine this resolution to determine whether they could be issued and we have found that conditions other than condition 3 are more restrictive and therefore we have used condition 3.

The Court: Have all the bonds been issued under this condition?

The Witness: I believe that that is correct, but I am not absolutely certain. My answer would be yes, within the context of this discussion.

The Court: Then would you explain the requirements of condition 3 which is the 1.3 test?

The Witness: Yes, your Honor, condition 3 is a protection with respect [516] to the issuance of debt by the Authority and it measures, in essence, two mathematical, ascertainable facts. One is what will

the debt service be in the maximum future debt serv ice year on—in this case, really, it is bonds secured by the general reserve fund.

Now, that means that you would take all of—if I may, may we talk in terms of today, of how this would work? We would take all of the obligations, bonded indebtedness, secured by the general reserve fund presently outstanding and determine what is the year in which the maximum debt obligation namely principal and interest is due because the bonds, whether they be serial bonds which come due at a particular time, or sinking fund bonds which require these sinking funds from time to time, term bonds, which have the technical due date, sometime in the future, and I think I have heard that described in court here before.

There are other obligations for payment of principal and interest and you may ascertain as a mathetical matter what year in the [517] future is the largest payment due.

That is a number, whatever it may be.

[518] The Court: All right.

The Witness: And that's throughout the one side of the equation. T 512-13 to 518-3.

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[521] The Court: All right. Now, you have explained then the one part of the equation is the maximum debt service requirement that you can project for the future.

The Witness: That's right. T 521-15 to 521-19.

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[522] Mr. Sovern: Excuse me, your Honor. I'm sorry for interrupting, but as I heard the testimony,

I want to be sure that I am clear about his. On the first part of the equation Mr. Zarin mentioned only the indebtedness already outstanding. Do you plan to come back with a new indebtedness or should that be pumped in at this point?

The Witness: I think that that is a [523] pertinent observation, your Honor, and that the obligations to be issued, also the debt service on those obligations also are to be included in the balance on the maximum future debt service side of the equation.

The Court: So it is plus the debt service requirement on the bonds to be issued.

The Witness: That is correct.

The Court: Okay. Now, does that complete the one side of the equation, of the formula?

[524] The Witness: It includes one side of the equation in the event the usual test with respect to the issuance of consolidated bonds under the 1.3 test is used; and the way we have usually used them is on the basis of the test of historical revenues.

The Court: Now we are on the other side.

The Witness: That is right.

The Court: Isn't that this formula?

The Witness: In this formula we have—

The Court: The revenues for your best twelve months out of the preceding thirty-six months—is that right?

The Witness: That is correct.

The Court: —must be equal to at least 1.3 times the maximum debt service requirements that you can project into the future. Is that it?

The Witness: That is the statement of the general rule under which we have been operating.

Excerpts from Testimony of Michael Zarin

The Court: Now, these revenues, do they include all revenues?

The Witness: The net revenues.

[525] The Court: Net revenues.

The Witness: Yes.

The Court: And that is from all facilities?

The Witness: That is from all current facilities of the Port Authority.

The Court: Does anybody have any questions on the 1.3 test? Or is there more to it?

The Witness: I think your Honor fairly stated it; there is more to the 1.3 test then we have just analyzed.

The Court: All right.

The Witness: There is more to the 1.3 test on the technical side, and there is, of course, a great deal more in terms of protections which it furnishes which we of course have not yet gone into. But in terms of the technical side of it, which I think your Honor is addressing at the moment—

The Court: That is right.

The Witness: —the 1.3 test also permits of certain estimates to be made under which the historical revenues which you have discussed may be augmented up to an amount equal [526] to 25 percent of the revenues which your Honor stated, that is the historical revenues, namely, the twelve months out of the next preceding thirty-six months, twelve consecutive months.

The Court: Up to 25 percent.

The Witness: That may be done in the event that there is a projection that the revenues to be derived from certain facilities for which the bonds are issued will actually be realized.

Excerpts from Testimony of Michael Zarin

The Court: Yes. You have to have a projection.

The Witness: That is right.

The Court: And if you have such a projection what you are saying is that you can include in the revenue part up to 25 percent of the projected net revenues.

The Witness: That is right. So that when you do that, as I was tossing this around in my mind thinking about it, if you are using historical revenues to the maximum, it is close to but not quite a one-times coverage test.

If you are using only historical revenues it is a 1.3 times test, because if you [527] use all of the historical revenues plus the 25, you are saying you are at 125 percent as against the 1.3 situation.

The Court: Right.

The Witness: And there is a thin margin over what we would call a one-times coverage in that situation. However, if you do include estimates you may also have to include on the original side of the equation additional bonds which are necessary to be issued in order to achieve those revenues. T 522-17 to 527-11.

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[528] The Court: If you ever use the project to augment your income then you would have to use the debt service requirements of the bonds that you will have to issue to achieve those revenues for the next three years. Is that right?

The Witness: That in essence is it. How the technical method would go and precisely which bonds they are is something we would have to analyze very closely. We have not done this really to any great

extent as far as that is concerned. Although we may have to.

The Court: Is there anything else about the 1.3 test we should know?

The Witness: Your Honor, if I may say so, that is the kind of question to which your [529] Honor subjected me when you asked me to appear to consider this matter independently with the respective counsel, almost word for word. I will answer your question.

The Court: No; in the context of this case, you know what the issues are.

The Witness: I understand.

The Court: Is there anything else that is important for us to know in the requirement of meeting the 1.3 test? Because up to this point I have a certain question which occurs to me, and maybe that will show you what I mean.

The Witness: Well, your Honor, we have addressed the technical provisions of the 1.3 test. The questions which I have addressed myself to have to do with what protection the 1.3 test affords.

The Court: Right.

The Witness: I will be glad to—how do I understand your question? How am I to understand your question?

The Court: Let me ask you a specific question and see if that sheds any light on what I really want to know.

Supposing the Authority wanted to issue [530] consolidated bonds in X amount to purchase a mass transit facility, and they projected a deficit for the foreseeable future with respect to that facility. How would you utilize that deficit in the 1.3 test?

The Witness: Your Honor, in my judgment the 1.3 test would in most cases not take cognizance of the deficit, because the 1.3 test is a protection against, in the context in which we have discussed it, general reserve fund bond maximum future years debt service.

So that certainly the particular obligation which was issued in order to commence an additional rapid transit operation, let's say of the type we are now working on in both the states of New York and New Jersey, the bonds to be issued at that time for that particular facility would be included as far as the maximum future years debt service is concerned. But the operating deficits and future issuance of debt for future capital expenditures in connection with that facility would not then be there. So it would just furnish as far as I understand it the limited protection with regard to the capital expenditures for which the [531] bonds are then being issued.

The Court: That is precisely what I am trying to find out: whether the 1.3 test furnishes any protection against the assumption of a huge operating deficit situation. And suppose you only had to issue $10 million in bonds, let's say, to acquire the Erie Railroad—I don't know whether the Erie is in bankruptcy or not, but let's make that assumption—or to acquire all of the commuter railroads that are operating in North Jersey; so your debt serivce requirements in this formula would not be particularly increased. But the operating deficit was $100 million a year.

Are you saying that you could nevertheless apply the 1.3 test using your historical earnings? And you

have no projected earnings to augment it; it is going to be a deficit. You apply the 1.3 test using your historical earnings to the bonded debt.

[532] The Witness: First of all, in answer to your question, I understand your question to be isolating it to the 1.3 test.

The Court: That is right.

The Witness: And recognizing that if 1962 will be applied to it, it would be one kind of thing, and all the other protections—

The Court: We are sticking in 1952.

The Witness: That's right.

The Court: Now we've got the consolidated bond resolution, and we don't have the covenant. All I want to know is whether the 1.3 test would preclude the Authority's assumption of a deficit operation.

The Witness: Your Honor, that would depend on the type of deficit operation concerned, how the Authority was going to assume the deficit operation, and the precise methods of doing it.

The Court: Well, take my hypothetical.

The Witness: Yes. If I were to answer your hypothetical question, it would be in answer—and I will answer it—to one method by which such a proposition might be presented. If I understand the particular [533] proposition which you were presenting, it is that you were undertaking the totality of a rapid transit system which has $100 million of deficits in a prior year.

The Court: Forget about that. Let's assume that the Authority is going to build rapid transit facilities throughout the meadowlands, and let's say Newark, et cetera; they are not going to acquire it from somebody else.

The Witness: What your Honor is describing now is akin to the connections of the Erie and Lackawanna and so on that are presently under contemplation and an extension of the PATH systems say down to Plainfield and that kind of thing which we are thinking about now.

The Court: Let's take it in two different phases. One is that they build a totally new facility.

The Witness: Right. Okay.

The Court: So it has no historical operating deficit as such.

The Witness: All right.

The Court: So you are going to build [534] that facility, and let's say it would cost you $10 million to build it, whatever it may be.

The Witness: Yes.

The Court: It may be a very small facility, but nevertheless it is a commuter transit facility, and you build it; you need to issue $10 million in bonds; and you can project—let's say you have $50 million in operating deficit each year.

The Witness: The 1.3 test, as I understand it, furnishes no protection in that situation.

The Court: That is what I want to know. You do not have to throw the $50 million operating loss into the equation when you are computing 1.3.

The Witness: That is my understanding.

The Court: Now let's assume that instead of building it they acquired the trackage for $10 million and that those railroads which were operating the trackage had a $50 million loss each year.

The Witness: Your Honor, if you were acquiring just the trackage—

The Court: —and the passenger cars, [535] similar to what was done with H & M.

The Witness: In the case of H & M, then we were acquiring an entire system.

The Court: Right.

The Witness: And in that situation, your Honor is saying that we would be operating the entire system as well, I take it.

The Court: Yes.

The Witness: Well, in that situation, which I am not sure that we have ever addressed before, that is an area—I am trying to define these areas where I have actual experience from those in which you are discussing in the situation.

The Court: Yes.

The Witness: And I am not sure that that situation even existed with respect to the H & M, namely, that it was operating at a deficit prior to the takeover.

The Court: Sure it was, wasn't it?

The Witness: No, I am not sure about that.

The Court: It was in bankruptcy.

The Witness: It was in bankruptcy, not able to meet its obligations. It was an [536] operation that consisted not only of the railroad operation but a number of other operations, also. And what was happening there—

The Court: Let's not go into detail with respect to it. Let's just stick with the hypothetical.

The Witness: In the hypothetical situation we would have to address the Condition 3, small Roman i, that in the case of facilities which have been in operation during the entire period of thirty-six months next preceding such time of issuance, we

would have to look at the combined net revenues derived from all such facilities.

There is an initial question which I would have to address if I were to examine this in an actual situation, whether the words "derived from" in that situation included a deficit or not.

If I did determine that it did include a deficit, which it may very well—as I say, that is something I really would have to consider, if it included a deficit in that particular small Roman i section, then obviously [537] we would be including those in that projection, if I came to that conclusion and so recommended and counsel for the Authority and others coincided with that judgment.

We are talking now in the case of the takeover of a complete facility operating at a deficit in the preceding thirty-six months.

The Court: Now you are not prepared or could not at this time express an opinion on that?

The Witness: Well, I think that, as I say, these are things I have been thinking about over the past few days and so on.

The Court: Yes.

The Witness: I think that if you are going to take over a whole operation, which is one of the possibilities, with that kind of a deficit you might very well have to include the deficits in that particular situation.

[538] The Court: Okay. Suppose you took over less than the whole operation?

The Witness: Your Honor, that goes to another type of question, which I am not addressing myself to, but which I have considered. T 528-10 to 538-6.

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Excerpts from Testimony of Michael Zarin

[540] The Court: All I want to know is, in your opinion, is the Authority required to include the deficit in its calculation to determine whether the 1.3 test has been satisfied?

The Witness: If we're talking about the deficits on an existing operation, which has existed in the past 36 months that's really the same question which we addressed ourselves to before.

The Court: You said if they took over the whole operation, in your opinion, they would have to include it. Now, we are [541] taking less than the whole operation.

The Witness: If they took over parts of the operation, which were deficit producing at that moment in time then—and having passed under the assumptions, the hurdle that we would include it in the deficits in the subdivision 1 the answer to that question would be yes. T 540-13 to 541-8.

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[543] [By Mr. Landis] Q. Mr. Zarin, does the 1.3 test really protect against deficit railroad financing by the Port Authority?

The Witness: Your Honor, the 1.3 test may be protective in certain very limited cases, but as I have examined it, I do not believe that it is protective against operating deficits. It is not protective in the situation in which your Honor outlined initially, namely the assumption of operation of a new facility and if I take protection to mean what I have listened to in the courtroom, what has been addressed to, namely protection of the security of bondholders, therefore it would not be protective in that situation and it would not be protective in my judgment in the event of the takeover an existing facility, if one

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were to approach that facility with the objective of bringing that facility within what we would call the general reserve fund family.

If you were to take it in particular ways, once you had taken it in even a limited [544] manner, there are some very real additional problems because the method of building a facility is not only a method through the use of the issuance of consolidated bonds. I really have—I think I have a few specific things in mind.

One would be the method of bringing in such a facility. I think, your Honor is correct in both assumptions which you addessed before the recess, namely if you were to assume an entire deficit operation at one time—as I say, I have never addressed this practically. If I had to address it, I think that fairly read you would probably have to include the prior deficits.

I could conceive a situation in which I would be pushed fairly hard on that question of if the Port Authority were directed to take something over because I would then be asked whether those were derived from, really mean only pluses, because in other cases, they do mean only pluses in this and other documents, but I think I would probably take the position in that situation that you would have to include [545] the prior deficits, and likewise in the situation which would be undertaking part of a facility which is operating at a deficit, but in thinking about the situation, I can see a possibility of taking on parts of an operation which were not deficit-producing as part of the Port Authority's obligations, and then taking on additional portions which

were deficit operations. If you did that, even if those deficits were to in a subsequent year prevent you from issuing any consolidated bonds, there are still sources of funds available to the Port Authority which could and probably would be used for the development of that facility and the payment of its deficits, funds which now stand as security for the bondholders.

Q. You are getting into then the flow of funds under the consolidated bond resolution, aren't you?

The Witness: When we —once we have issued an obligation for a facility, then all of the convenants and the flows of funds apply to that facility.

The Court: I realize that, yes.

[546] The Witness: Now, so that part of it does have to do with the flow of funds.

That part that I am talking about has to do with, for example, and it is a dramatic example, is the one that occurs to me, is that if you wanted to assume —you being the Commissioners of the Port Authority—wanted to assume the development and operation of, say, the Second Avenue subway which is not yet in operation, there being no deficits, operating deficits on that facility, and say the prior bonds being the obligation of the Transit Authority or the City of New York, you could, absent all other protections which exist, which we are not talking about, probably undertake that portion of that kind of deficit operation.

Having undertaken that portion of the deficit operation of the subway system, we are bypassing right now, whether other covenants, which we will get into,

Section 7 and Section 6 of the statute, might protect against that, but having taken that as part of the general reserve fund family under the 1.3 test which we are addressing now, the [547] hypothetical situation in which—which you have addressed in the past days and which we have addressed from time to time at the Port Authority in thinking about what are the perimeters of this thing, the rest of the system, there being now a facility on the Port Authority's books dealing with the rail situation, there is nothing under the 1.3 test which would prevent the balance of that system from being given to the Authority without the issuance of any obligations, thus incurring even a more—well, and obviously a type of deficit that would be more substantial.

In my judgment, for that reason and for a number of other reasons, if we are talking in terms of what the protective perimeters are of the statute so far as someone working with it, with an objective to bring into it, and let's even put the New York City subway to the side for a moment, if you have an objection to bring into the family substantial deficit operations, it is not the 1.3 test which furnishes the protection, whether with respect to railroads or with [548] respect to facilities of any other type.

The 1.3 test, if I were to ask a lawyer in my division to bring—to somehow bring within the family such a facility without looking at anything but the 1.3 test, I would feel that he was not being appropriately creative if he could not figure out some way to do so. T 543-2 to 548-9.

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Excerpts from Testimony of Michael Zarin

The Court: Well, now, in that connection, the legality of the issue of the bonds under the consolidated bond resolution, which is the only time the 1.3 test comes into play when you go to issue a bond—

The Witness: The 1.3 test comes into play at the time of issuance.

The Court: The legality then of the issuance of the bonds is passed upon not only by Mr. Falvey, the general counsel of the Authority, but also by bond counsel.

The Witness: Yes, sir.

The Court: So that you not only have to think of some ingenious way of circumventing the intent and purpose of 1.3 that satisfies Mr. Falvey, but you have to satisfy somebody [549] else.

The Witness: That's correct, your Honor, and as far as the 1.3 test is concerned, I would not deem that to be a difficult job. T 548-11 to 549-5.

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[551] [By Mr. Sovern] Q. Let's take the hypothetical you gave of the Second Avenue Subway in which first the Port Authority, through the issuance of consolidated bonds acquires some non-deficit producing—well, it would [552] have no deficit because it has no operations, and then becomes the proprietor of the entire subway system. You said 1.3 test provides no protection against that. I understood that very literally, that is to say it provides no protection against that in the sense that by itself at that moment it provides no protection. But if that event were to occur and at any time thereafter the Port Authority sought to sell consolidated bonds to finish the World Trade Center or improve LaGuardia Airport or put new toll booths on the Washington Bridge would the 1.3 test apply

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to that issue of bonds? A. Somehow, Mr. Sovern, we would find a way to build those toll booths, but apart from that I think your statement is quite correct. When you—

> The Witness: And that's one of the reasons, your Honor, that the 1.3 test has a little bit of unreality to us, because the—if we can't meet 1.3 with respect to the issuance of consolidated bonds our operations, as far as their financing to consolidated bonds are at a standstill.
>
> So really just to meet the 1.3 is not, is not—is skating very close to the point of stagnation for the organization, • • •. T 551-22 to 552-24.

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[556] Q. All right. Let me ask just a couple of other questions. I take it that the point at which Mr. Falvey came to you and said, "Tell me, Mike, whether we can do the Second Avenue Subway and the New York City Transit System this way", you would say, "We can do it, but that's the end", is that correct? A. Oh, absolutely not. I would certainly not say that at all.

Q. You would not say that? A. I would not say that in that manner at all, nor would he address it in that way. T 556-1 to 556-12.

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[557] Q. (Continuing) If we bring into the general reserve family a facility with a 300 million operating deficit, that deficit will have to be calculated in the next time we come to issue bonds and apply the 1.3 test. Is that correct? You would so advise him. A. Mr. Sovern, that's not the way I give advice. And if you want to address the question with respect to the various hypotheticals we're giving here, that's one thing, but I—to answer that question, I would have to go into areas which are—the first thing I

would talk about would be, [558] for example, basic covenants and Section 7 and whether it's a good idea and lots of other kinds of things, but that's not what you are addressing.

> The Court: All we want though, Mr. Zarin, is your opinion, not how you would advise a client who is pushing you, but your opinion as to the interpretation and effect of the consolidated bond resolution on these various hypotheticals. T 557-14 to 558-9.

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[559] [By Mr. Sovern] Q. When you said that the 1.3 test provides no protection in this situation, there they are referring to the building of a new facility or a sort of acquisition of their Second Avenue subway which you hypothesized, when you said the 1.3 protection—I'm sorry, the 1.3 test provides no protection in this situation you are looking at that very limited moment in time without reference to future actions of the Authority in answering the—you were being very literal. Is that correct? A. I was answering in two respects. One in point—in that point of time; secondly, with regard to the limited period of, call it the next three years, which we could analyze out.

And now your question takes me to the point beyond that and saying, "What protection would the 1.3 test then provide?"

And what would happen in that situation is that if there were another occasion to issue consolidated bonds and the maximum future years debt service was exceeded—I beg your pardon—and the maximum future years debt service was—

Q. Off the record, you have to turn [560] that sentence around. A. All right. If the net revenues of the Authority as we have discussed them including such estimates as we might bring into that situation did not equal or exceed 1.3

times the maximum future year's debt service, at that point the Authority could not issue a consolidated bond.

Now, that does not mean, however—your Honor, this does get slightly out of 1.3, but I think you are talking about whether 1.3 is protective of the securities. That does not mean, however, that the security of the bondholders is protected because you have brought this deficit operation into the family of facilities.

Being a member of the family it must be nourished. And the general reserve fund and the consolidated bond reserve fund would then nourish that new member of the family, because they are required to.

If the deficit was as large as you postulated it to be the general reserve fund and the consolidated bond reserve fund would be—

Q. Last about six months? A. It would last a very short time.

Now, that's not only to speak of the deficits [561] because if we did undertake that kind of operation we have an obligation under the miscellaneous covenants in Section 12 to complete that facility.

> The Court: Mr. Goldberg, I think, said that perhaps, if you get the disease in your system you may die.
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> The Witness: Judge Gelman, I'm really sorry in a way that that remark is on the record, because I've devoted considerable part of my professional career to trying to help in bringing into the Port Authority, in a method which would be satisfying to both the bondholders and to the public need for transportation, mass transportation. And I certainly do not consider it to be a disease at all. T 559-2 to 561-16

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Excerpts from Testimony of Michael Zarin

[562] By Mr. Sovern:

Q. To come back to your sequence of events then, this massive deficit is in the general reserve fund family of facilities. It prevents the Port Authority from issuing any further consolidated bonds, because the 1.3 test cannot be met. The consolidated bond reserve, the general reserve fund are then totally absorbed by the deficits. Then what happens? A. Well, then we can't pay the bondholders. And the first bondholders whom we cannot pay—in that situation which is again, we are addressing only the 1.3 test protection, we are not addressing the protections of the 1962 covenant, and so on. And I make that statement very clearly, your Honor, because of the next statement that I am going to say, which is that I am not saying this protection does not—is not currently protected in other ways.

The protection may very well exist in other ways, but under this hypothesis which is presently theoretical, sixteen major banks in the New York Metropolitan area would have no source of payment for over 200 million in bank loans. T 562-2 to 562-25

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[563] Q. All right. I don't want to get us into that byway, but what I do want to conclude on this line of inquiry is I take it that if there were propositions put before the Commissioners by anyone, and anybody who was disposed to take it seriously, you would, and I don't now propose to stipulate the form in which you would give it or [564] what else you would say, you would advise your superiors that they might have before them this probable series of events, as a consequence of the proposed action. Is that correct? A. If we were going to take the actions precisely along the lines that we have hypothesized, and with the

Excerpts from Testimony of Michael Zarin

particular deficits that we have hypothesized, and so forth, I would so advise. T 563-20 to 564-8

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[567] Q. May I ask, you described the 1.3 test as mathematical and precise when dealing with both the calculation of the maximum debt service and the historical revenues. Then you went into a discussion of the possible inclusion of estimates of up to 25 percent more of additional revenues from the facilities that were not operational at the time of the issue. How were those estimates made? Are they made with great care? A. Mr. Sovern, I do not make those estimates. I believe them to be made with care.

The Court: It is the professional staff of the Authority which makes the estimates.

The Witness: Yes, that is right, your Honor.

Q. And outside consultants are consulted as well? A. To make those estimates?

Q. Yes. A. I would say that would not usually be the case.

Q. But it is the professional staff of the [568] Authority that does that estimating? A. That is correct. T 567-4 to 568-2.

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[By Mr. Landis] Q. In response to Mr. Sovern's question about the 1.3 test you indicated the need to nourish a facility in the consolidated bond family. Would you be specific about the source of that requirement and describe it in more detail?

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[569] The Witness: We are not talking about flow from the general reserve fund or anything of that sort, but just on Page 67 of the official state-

ment that we are talking about, there is a Section 12 called "Miscellaneous Covenants." I was referring to Paragraphs [c], [d] and [e] which reads as follows. The introduction I should say to all of these is:

"The Authority covenants and agrees with the holders of Consolidated Bonds, and with each such holder, as follows." And then skipping [a], talking about performing all duties required by the Constitutions and so forth and others, to [c]. [c] reads:

"To proceed promptly and in an economical [570] and efficient manner with the effectuation, establishment, acquisition, construction, rehabilitation or improvement of all facilities, the effectuation, establishment, acquisition, construction, rehabilitation or improvement whereof is financed with Consolidated Bonds."

Mr. Landis: Or if you could not finance it with Consolidated Bonds.

The Witness: That is what I was addressing, if you could not do that you would have to look—it is a covenant, to proceed. So you would look to see whether you had any other source of funds.

Once having financed a portion of the facility with Consolidated Bonds, and covenanting to proceed promptly with the effectuation of the facility which is financed with Consolidated Bonds, we would look to another source, or could continue.

But I am also referring to Subsection [d] which says:

"To maintain in good condition all facilities the surplus revenues of which are payable into the General Reserve Fund, and to operate them in an

efficient and economical [571] manner, making all such renewals and replacements and acquiring and using all such equipment as the Authority shall determine to be necessary or desirable for the proper and economical maintenance and operation thereof."

And [e]:

"To make such improvements as part of or in connection with facilities the surplus revenues of which are payable into the General Reserve Fund as the Authority shall determine to be necessary or desirable as incidental to or in connection with the operation of said facilities."

I perhaps should not have used so imprecise a word as nourish, but I think that perhaps is descriptive when considered along with another term which I used, namely, bring the facility into the family. T 569-11 to 571-18.

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[573] The Court: I would like you to describe the flow of funds under the consolidated bond resolution prior to the enactment of the covenant.

The Witness: When your Honor speaks of covenant—

The Court: Or as it would occur without the covenant—as it would occur today without the covenant.

The Witness: When your Honor speaks of covenant, I take it you are speaking of section 6 of the 1962 legislation.

The Court: That is right, exactly. And let's take it as of today, assuming that there is no covenant that is in effect.

The Witness: The flow of funds with respect to the consolidated bond resolution is the same as the

flow of funds which I have described with respect to the general and refunding, Air Terminal and Marine Terminal Bonds, with the—

The Court: Let's see if I understand it. You collect all of the revenues from all of the facilities of the Authority. Is that right?

The Witness: Yes.

[574] Mr. Sovern: If I may, your Honor, for which consolidated bonds have been issued. Is that not correct?

The Witness: The flow is the same. Mr. Sovern is correct with respect to the facilities, and as your Honor well knows, the Air Terminal Bonds, or the Revenues were flowing from the particular facilities and the others from those faciilties, and so on.

The Court: But not any more.

The Witness: Now, when I said the same, I meant all of those facilities and any facilities constructed since then, because having placed to one side the prior lien bonds then all the facilities are within the consolidated bonds family.

The Court: I am looking at the Pledge of Revenues under section 4.

The Witness: Right.

The Court: You have pledged the revenues from each of the following, and you list all the facilities. Are there any facilities owned and operated by the Port Authority other than those described in subparagraph i?

Mr. Laulicht: Either under i or under ii?

[575] The Court: I understand.

Mr. Laulicht: Because PATH and World Trade Center would come under ii.

The Witness: It isn't only PATH and World Trade Center, it is also the new passenger ship terminal.

The Court: So it is all facilities presently owned and operated by the Authority.

The Witness: It is all facilities, your Honor.

The Court: You take the net revenues from those facilities.

The Witness: That is correct.

The Court: Now, PATH is presently operating at a deficit, is that right?

The Witness: Yes.

The Court: And I assume that the World Trade Center is operating at a deficit, is that right?

The Witness: I am not sure that that is the case, your Honor. I don't believe that the World Trade Center is operating at a deficit.

Mr. Landis: Your Honor, I believe that is in the stipulation, and I believe for the year 1973 as stipulated, the stipulation is [576] that there were net operating revenues from the World Trade Center.

The Court: That there were, okay. Then forget about the World Trade Center.

Now, when you start moving the funds around, do you shift funds over to PATH first before you calculate your net revenues?

The Witness: Your Honor, we are at another one of those questions to which I have not been asked—

The Court: Just express an opinion as to how it is supposed to be done.

The Witness: These net revenues as far as these particular facilities are concerned, whether you treat them as being satisfied before net revenues or after net revenues, the year end results for the Port

Excerpts from Testimony of Michael Zarin

Authority, that is to say, what its results from operations are, what the status of its reserve funds are, and so forth, are exactly the same whether you have in fact satisfied the deficit, say, move the money before or whether you move the money afterwards, the result is precisely the same result.

The Court: All right. Then the net revenues are applied to debt service on the [577] consolidated bonds.

The Witness: Yes. Your Honor is putting it in the framework of what it is we do today, is that right?

The Court: What do you do today?

The Witness: We do that, and let's say that today just for the sake of setting the framework is December 31 of any given year, because that is a day on which we can best describe this, within that time.

The Court: All right. You pay the debt service on the consolidated bonds.

The Witness: The debt service on the consolidated bonds would be paid.

The Court: Now, what do you do with what is left over? T 573-1 to 577-16.

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[578] The Witness: It goes to the general reserve fund within that context.

The Court: Up to the 10 percent figure, is that right?

The Witness: That is correct. Actually, if in a particular year the reserve fund were full then nothing goes to it.

The Court: Sure. Then it goes into the consolidated bond special reserve fund or—

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The Witness: Called the consolidated bond reserve fund.

The Court: Now, as I understand it, there is no limit on the consolidated bond reserve fund. In other words, it does not have to be maintained at any specified level. It is whatever is left. Is that right?

The Witness: That is correct, your Honor.

The Court: Now what are the charges on the consolidated bond reserve fund? That is, what is it pledged to?

The Witness: Your Honor, the consolidated bond reserve fund is treated at Section 7 of the consolidated bond resolution appearing on Page 64 of the official statement with respect to the [579] 41st series of consolidated bonds. I think your Honor referred to that as Exhibit II.

The Court: That is Exhibit II annexed to the the stipulation.

The Witness: Yes.

The Court: Now, would you explain that and particularly what may be paid out of the consolidated bonds reserve fund?

The Witness: Yes, your Honor. The section begins by describing the funds and the payments into the fund; that is what we have already discussed.

The Court: That is right.

The Witness: And then the purposes to which the fund may be applied are listed. The first is the payment of consolidated bonds at maturity under certain conditions. So I take it that your Honor wants a brief description, and that has to do with the payment of bonds.

The Court: That is right.

The Witness: (b) has to do with the payment of debt service on consolidated bonds.

(c) has to do with the purchase for retirement of consolidated bonds.

(d) has to do with the redemption of [580] consolidated bonds. I will read (e) if you would like.

The Court: No, it is not necessary. Here is where you can pay expenses.

The Witness: I just meant that this was more than those rather than formal and obvious ones.

The Court: That is right. Here you can pay expenses for the operation of any facility where the net revenues of the facility so long as they were pledged as security for consolidated bonds, to the extent that the gross operating revenues of that facility are insufficient.

The Witness: Yes, your Honor.

The Court: Here is where deficit operation would be subsidized by consolidated bonds.

The Witness: Consolidated bond reserve funds.

The Court: By consolidated bond reserve funds.

The Witness: That is right.

The Court: So accountingwise when we are talking about whether you go up and then come [581] back down to the deficit operation; actually, the way it is literally applied, even though the result may be the same, you are supposed to take the net revenue from each facility and flow it through into the reserve fund and then pass it back to the deficit facility. Is that correct?

The Witness: Your Honor, I am not sure that that is correct.

The Court: All right. Now, [f] is what, the payment of debt service on bonds other than consolidated bonds? We are on [f] now on Page 65.

The Witness: Yes. [f] says: For the payment of debt service on bonds other than consolidated bonds which are described in the last paragraph of this Section 7. And that one states that the pledge made is subject to the rights of the Authority to issue bonds other than consolidated bonds secured by a pledge of or lien or charge upon the consolidated bond reserve fund prior to equal to the pledge, lien and charge in favor of consolidated bonds, only if those bonds are issued to fulfill obligations undertaken for the benefit of the holders of consolidated bonds and if they are also secured by a pledge of the general reserve fund.

[582] The Court: All right. Now, supposing the Authority issues a different class of bonds other than consolidated bonds, you say mass transit bonds, and you incurred this deficit, could the Authority use monies in the consolidated bond reserve fund to pay that deficit?

The Witness: Your Honor, without the protection of any other covenant, statutory or under the bond indenture, but just looking at this section, we are not even going to other parts of this resolution, but just under this particular section and not going to any other statutory material at all, this particular section might permit that kind of a bond, that is again an issue that I would want to sit down and consider carefully which we have not had, but I think that we have not had such a bond, but I think that under this particular section, you could so construct such a bond.

The Court: Which paragraph, F or G?

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The Witness: Well, more certainly under—more certainly under G than F, but under F probably with respect to, say, you were talking—you were talking about a railroad, [583] if I understand you correctly.

Under F, probably with respect to PATH, which is a general reserve fund facility.

The Court: Well, PATH bonds are consolidated bonds, aren't they?

The Witness: Your Honor, I believe asked me whether we could issue an additional type of bond.

The Court: I see what you mean, it would be for the benefit of the holders of consolidated bonds?

The Witness: Yes, sir.

The Court: Now, going back to section four, maybe this obviates the question, but the question I was going to ask was assuming that the Authority never issued a bond for the purpose of engaging in a mass transit operation, but acquired the facilities by way of gift of otherwise, would the Authority be able to use the net revenues annually or funds in the consolidated bond reserve fund to pay deficits in that facility.

The Witness: That is a question which we have addressed, thought about some, and if I understand that correctly, I have to know whether [584] you want me to answer only within the perimeters of section 7 of the consolidated—if I may, your Honor, we are about to embark on some wholesale confusion with section numbers—I am speaking now—

The Court: Let's take section 4, first.

Mr. Sovern: I wonder if the witness could first state his conclusions and then give us the answer.

The Court: Why don't you give us an answer to the question.

Excerpts from Testimony of Michael Zarin

The Witness: I will, your Honor.

The Court: Yes, no or maybe.

The Witness: If we were talking about the section 7 of the consolidated bond resolution adopted in 1952, subparagraph G provides that.

The Court: Can you answer the question yes or no, first, and then explain why.

The Witness: In my opinion, deficits could, if confined just to the section, be satisfied out of the consolidated bond reserve fund. T 578-1 to 584-22.

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[593] The Court: All right.

Now, if you look at page 22 of Mr. Goldberg's remarks.

The Witness: Yes, sir.

The Court: Beginning with the first full paragraph on that page, the second sentence of that paragraph, he says, "All the revenues were pledged to particular families of bonds; all of them had to be used either to pay —", and so forth.

And the next paragraph he says, "You could not make the claim that reserve fund expenditures would maintain or enhance the security of our bonds if the money was to go outside of the P.A. families, as was proposed in one suggestion that we simply subsidize the private railroads to the extent of their commuter operating deficits."

[594] Now, is his position as it is stated here inconsistent with what you have—with the opinion you have just expressed?

The Witness: No, your Honor.

The Court: Well, could you explain how you reconcile what you said or what you have just testified to and what he says here?

First of all, do I understand you are still talking only about the consolidated bond resolution of 1952?

[595] The Witness: Your Honor, Mr. Sovern stated before you commenced this line of questioning that the next step that we would undoubtedly be considering is Section 7 of what it is that we call the series resolution.

By that I have reference to the resolution contained in the official statement which we have been considering at Page 72, entitled "Resolution Establishing 41st Series of Consolidated Bond Resolution, Due 2008, Section 7."

The Court: Section 7 certification?

The Witness: That is correct, Section 7 appears on Page 76 of that statement.

The Court: But if you follow Mr. Goldberg's remarks on Page 22, he is talking about the situation as it was prior to the adoption of the Section 7 certification in which he says commenced with the 12th series of consolidated bonds.

The Witness: Mr. Goldberg goes on, your Honor, immediately thereafter to speak of a fear in the financial community and I think that Mr. Goldberg is speaking, as well, with the benefit of Section 7 of the consolidated [596] bond series resolution in mind.

The Court: Well, that is not the way I read his report.

Mr. Sovern: I think I can clarify it. Mr. Goldberg is referring to the decision, 1958, of the Section 7 certification. That is to be found in Paragraph 2 of Page 76.

I assume that I would ask the witness to correct me if I am wrong, that the first paragraph of Section 7 has been there for some time. Am I correct?

The Witness: Mr. Sovern, I had been sitting here thinking about how I was going to ask you if you had a copy of the consolidated bond official statement with regard to the 11th series of bonds. May I see that, if you have it?

Mr. Sovern: I am afraid I do not, that is why I was stating an assumption rather than a fact.

The key point, your Honor, is that there are two protections in Section 7 that we are talking about, in the series resolution.

The Court: All right.

So, now, let's move from the '52 [597] resolution to the series resolutions.

The Witness: The ones which I previously identified, and also this resolution, Section 7, that I have spoken about in the series resolutions, is, as I understand it, consistent in issues of Port Authority obligations, consolidated bonds and notes, from the 12th series on so that that is what we are talking about.

The Court: What about the first paragraph of Section 7?

The Witness: I had wanted to take a look at it. I am not certain whether it is or is not in that as well, but it certainly is consistent, the 12th series, and if we take this in terms of your Honor's statement this morning with reference to where we are today, it certainly is here today and has been through the period which you are addressing yourselves, namely, 1960, '62 and on.

The Court: Section 7 has not changed, then, from the 12th series on?

The Witness: That is my understanding.

The Court: Now, does this provide for any limitation the use of consolidated bond reserve funds to pay the operating deficits [598] of a facility acquired without the issuance of consolidated bonds?

The Witness: This does not permit such application.

The Court: What language specifically contains the prohibition?

The Witness: Section 7 states the Authority shall not apply any moneys in the consolidated bond reserve fund or in any special reserve fund established for the benefit of bonds of any prior issue except for the payment of bonds secured by a pledge of the general reserve fund in whole or in part.

The payment of debt service upon bonds so secured, then without reading the whole of it, your Honor, it goes on to speak only of undertakings with respect to bonds secured by a pledge of the general reserve fund, in whole or in part.

If I may, your Honor, could I heard your question, because I assume that you are going to ask a series of questions based upon it. May I hear your question that you raised?

The Court: Yes.

[The reporter read back as requested.]

[599] The Witness: Your Honor, there is here with regard to Subdivision [g] an area which we have not specifically addressed at the Port Authority which would raise a question in this regard, namely, could you apply moneys under Subdivision [g] from the consolidated bond reserve fund for bonds which

are general reserve fund bonds, but not consolidated bonds, and that would not appear to be proscribed.

If I take your Honor's question to include when you say without the issuance of consolidated bonds to mean without the issuance of bonds backed by the general reserve fund, the answer would, I think, be completely accurate in regard to my understanding, but it is perhaps in the present context, a distinction without a difference.

By Mr. Sovern:

Q. I take it the key point in Section 7 of the [Series] Resolution, plungs the gap you identified in Section 7 [g]of the consolidated bond resolution? A. Well, Section 7 in its totality—

The Court: Not just the first paragraph? I thought you derived that from the [600] first paragraph, that is why I said—

The Witness: If the gap be defined as whether you could issue bonds extraneously or just—

Q. As I understand the gap, what we have been talking about is the white elephant hypothesis—that is to say, a gift of a facility, deficit-generating mass rail transit is made to the Port Authority and the question is may the consolidated bond reserve fund be used to pay the operating deficits of that enterprise and the question I need to put is to the extent that 7[g] permits that, does not Section 7 of the series resoltuion preclude it? A. In order to bring a facility, without characterizing it, into the family of facilities, one would have to issue an obligation secured by the general reserve fund.

Mr. Sovern: Thank you.

[601] The Court: Now that much is contained in the first paragraph of Section 7.

The Witness: I believe that is so, your Honor.

The Court: Now we will get to the second paragraph of Section 7 which we have been referring to here as the Section 7 certification.

The Witness: Would you like me to describe that at this time?

The Court: Yes. What is the certification which the Authority must issue before it can authorize the issuance of further consolidated bonds?

The Witness: Your Honor, Section 7 certification contained in Paragraph 2 is a certification which must be made by the Authority prior to the issuance of Consolidated Bonds or at the time of the issuance of Consolidated Bonds for the application of the funds.

That certification consists of the opinion of the Authority that the issuance of the bonds or the pledge of the General Reserve Fund as security for bonds other than [602] consolidated bonds will not, during the ensuing ten years or during the longest term of any of such bonds proposed to be issued [whether or not consolidated bonds], whichever shall be longer, in the light of its estimated expenditures in connection with such additional facility or such group of additional facilities, materially impair the sound credit standing of the Authority or the investment status of consolidated bonds or the ability of the Authority to fulfill its commitments, whether statutory or contractual or reasonably incidental thereto, including its undertakings to the holders of consolidated bonds.

Those are substantially the words behind it. But the meaning behind it, and what happens with respect to an additional facility is that that facility

coming into the group of facilities with the first issuance of bonds, for example, a new passenger ship terminal or whatever you might consider, is analyzed and judgment made, assuming we are to go ahead with it, that issuing bonds for that facility and bringing them within the family will not impair the credit of the entire enterprise.

[603] That I think is the most important concept of this judgment which is made as to whether or not the facility should be taken into this group.

The Court: Well, that is not the only certification that is required.

The Witness: Your Honor has reference to—

The Court: Impairing the sound credit standing of the Authority or the investment status of the Consolidated Bonds—is that right?

The Witness: That is right.

The Court: —or the ability of the Authority to fulfill its commitments. Now I can appreciate—

The Witness: When I said impair the standing, perhaps I abbreviated too much. I meant to read the word hereafter to refer to them.

The Court: But do I understand correctly that before the bonds can be issued under such a resolution the certification must be made that all three conditions that are set forth in this sentence must be met?

The Witness: Oh, yes. There would, if [604] the commissioners decided to go ahead with a new facility in this way, be a resolution adopted which would so provide.

The Court: Now forgetting for the moment what the words impair the sound credit standing of the

Authority may mean; what do the words investment status of consolidated bonds have reference to?

Is that to the Moody's or Standard and Poor's rating? Is it to the question as to whether they are legal for investment purposes for trusts and so forth?

The Witness: Your Honor, I have given some considerable thought to the meaning of this over the years, and also since Monday afternoon when I was asked to come down here.

What your Honor has asked is a very difficult question, because this particular section is quite different from some of the other sections which we have discussed, say the 1.3 test and so forth, where there are mathematical computations to be made.

In my opinion this section permits of a range of possible answers to your question. And the range of possible answers to the question [605] of what the investment status means, and many of those other phrases in the section would range from the commissioners' or a commissioner's judgment—because I assume that each one would think about this thing individually and get the benefit of the group's understanding as well—would range from a commissioner's judgment that he thinks that there will be over the years sufficient amount available from all of the sources that we have discussed to pay principal and interest when due on the bonds, all the way through the other protections which we have. For example—

The Court: Are you going behind the words investment status?

The Witness: No, your Honor.

The Court: You are just confining it to investment status?

The Witness: Yes.

The Court: Does investment status have reference in your opinion to a Moody's rating or a Standard and Poor's rating?

The Witness: Your Honor, I did not draft this resolution. Investment status means what it is which affects the bonds as far as our [606] ability to issue the bonds is concerned and its market relationships to the bonds and so forth.

It takes in the whole area of an investor's willingness to buy our bonds. It takes in the whole area of what happens to those bonds in the hands of the investors.

And that is why I say that judging from all of the things that I have read and listened to, different individuals have different ideas about that which are not encompassed solely within Moody's rating.

Some people indicate—when I look at this I have to look at it from the standpoint of an analyst looking at what other components are making up the investment status of Port Authority bonds. What is it that makes them what they are?

The Court: I take it what you are saying is that there are no objective criteria or no single criterion.

The Witness: No single criterion. If you would like the benefit of my thinking on it, what the criteria are, not generally, but just Port Authority bonds, they would range from, as I say, just the payment of principal and [607] interest through the kinds of things that we were discussing this morning, namely, would the issuance of such a bond impair the ability of the Authority—

The Court: To fulfill its commitments?

The Witness: Right.

The Court: All right. Now, as to that phrase—

Mr. Sovern: Which phrase, your Honor?

The Court: The ability of the Authority to fulfill its commitments. If the Authority were contemplating the issuance of consolidated bonds for the acquisition of or the construction of a mass transit facility, and the projections made by the Authority showed let's say an operating deficit of $100 million a year for the next ten years; in your opinion could a commissioner or could the commissioners issue a certification satisfying the requirements of Section 7? And here we are today, and assuming the Authority's financial statement as it presently exists.

The Witness: Your Honor, that would require an answer which I would need and would ask in that situation if that was presented to [608] me, that here we want to take on this particular deficit; I think the commissioners would also be interested in projections of revenues from other facilities.

The Court: Of course.

The Witness: And so we would be speaking not only of today's statement but rather our analysis of where we would be over the next ten-year period.

The Court: Right.

The Witness: So, for example, if a commissioner were to state or in thinking it through himself, or whoever was judging this thing also to feel that revenues were to be substantially increased over the next ten years; the answer to that question might be under Section 7 that it would be suitable.

For example, and again we are talking about—

[609] The Court: He couldn't just sit there and turn his head upwardly and say, "Yes, I think we're

going to have enough money." He'd have to base it on some objective projections that were made by somebody.

The Witness: Your Honor, that's exactly what happens.

The Court: What?

The Witness: There are projections made.

The Court: Right.

The Witness: For example—

The Court: Hasn't it been the practice heretofore in connection with the issuance of consolidated bonds since this Section 7 certification requirement has existed that the Commissioners have presented to them by the staff of the Authority who are responsible for making those projections a set of projections which shows what the anticipated revenues will be over a ten-year period, at least ten-year period, and what the debt service requirements will be, etcetera, so that they can make this certification?

[610] The Witness: Your Honor, just such a certification was made in connection, for example, with the undertaking of the Hudson Tubes, and in that situation the Commissioners anticipated that there would be a deficit of between 5 and 6 million dollars, which they could accommodate within the family.

They also anticipated that there would be, in their judgment, not looking up to the sky, but looking at analysis, that all of the future deficits of the 5 to 6 million dollar amount would be accommodated through fare increases and made their certification on that basis.

The Court: Well, you see now that sounds slightly partisan, if you don't mind my saying so, because that's not the question which I asked. All I

asked was that heretofore with respect to any issue, whether it was PATH, whether it was World Trade Center or any particular issue, the Commissioners sit with projections in front of them before they made such a certification.

The Witness: Your Honor, if that was [611] a partisan statement I beg your pardon. It was intended as an example, and I had another example in mind.

The Court: No, I don't want examples. All I want is to know what the practice has been? Has that been the practice or hasn't it been?

The Witness: The practice has been as I described it.

The Court: They do have the projections?

The Witness: The Director of Finance will make certain projections and assumptions which he will present to the Commission.

The Court: So the accuracy of those projections, and here the certification, will depend, presumably, upon how good the people are who made the projections and the assumptions which they used. Right?

The Witness: I don't think it depends entirely on the people who have made the projections, your Honor.

The Court: Well, I only meant that in the sense that—

The Witness: It has to do with what [612] then happens over things which such people may or may not have control over. For example—well, I'm sorry.

The Court: But presumably there is as objective a set of facts, projections in front of the Commissioners as you can get. Is that a fair statement?

The Witness: Your Honor, it's going to be difficult for me to discuss this without any examples whatsoever.

Let me take bridges and tunnels as an example, if I may.

The Court: All right. Why don't you take the second deck of the George Washington Bridge.

The Witness: All right. Well, with respect to the second deck of the George Washington Bridge or with respect, say, to a resurfacing of the bridge, which we now are thinking about, we may have a need. This is also hypothetical. Okay? We may also have a need to have additional revenues in order to support that resurfacing of the bridge.

In that situation you might project that an increase in bridge and toll revenues, [613] bridge tolls would be adopted by the Commissioners and approved by the Governors and accepted without challenge by the Department of Transportation, which has the ability to determine the just and reasonable tolls over the bridge, or you might have something more definite involved.

In such a situation as this, a Governor may have given an assurance that he would not veto such an action, or the Department of Transportation may have analyzed it.

The Court: Let's not get involved with those matters, please. And I would prefer staying with something which actually happened. They did put a second deck on the George Washington Bridge.

The Witness: Right.

The Court: That was done. That was financed through the issuance of consolidated bonds, wasn't it?

The Witness: Right.

The Court: Now, before the Authority issued the certification required for the bonds, I assume that the staff prepared [614] projections showing what the additional income would be as the result of the installation of the second deck on the bridge?

The Witness: Well, your Honor, I'm sure there were projections, but there were not projections under this section.

The Court: Well, don't they have to have them, that's all?

The Witness: No, your Honor.

The Court: Well, what was the past practice of the Authority?

The Witness: The only past practice to which I may refer, your Honor, are things to which I have alluded such as the PATH certification and passenger ship terminal because the second deck of the George Washington Bridge is a matter with respect to an existing facility. And this certification need be made only the first time bonds are issued for a facility, not each time bonds are issued. This is as distinguished from the 1.3 test which must be satisfied each time consolidated bonds must be issued.

[615] The Court: All right. I've got it. I've got your point. But with new facilities, then, that were issued and which were constructed and financed through consolidated bonds, wasn't it the practice of the Authority to waive the objections made to determine whether or not the issuance of the bonds would impair the ability of the Authority to fulfill its commitment to the holders of consolidated bonds?

The Witness: Your Honor, those projections were made. However, in the— and I don't mean that they

were not made carefully. I assume they were made carefully. But in the actual practice of making such certifications under Section 7 there was at the time those certifications were made, not describing it, your Honor, but with respect to PATH or other of the facilities which were certified, some heliports and other kinds of things, and there have not been a great number of these because you will recognize that many of the facilities were in place before that. There was reasonably wide latitude when considered as part of the [616] revenue flow of the entire Port Authority. So that a Commissioner focusing on this might be wrong within a very wide latitude of millions of dollars as far as an exact projection is concerned and still be perfectly right with regard to this provision because the provision might not cut in at all points along the way.

If you say that as part of the investment status of Port Authority, you will consider something that we have not yet talked about, for example, the policy of the Port—

[617] The Court: I just want to dwell on this one phrase for the time being and see if I can understand what is required of the Commissioners in order to make the certification, and as I understand it, and maybe I don't understand it, they do have projections, don't you agree?

The Witness: Yes, your Honor.

The Court: And do those projections show that within the ten-year period by reason of the operating deficits that would be incurred by this new facility, the Port Authority would have depleted its consolidated bond reserve, it would have depleted the general reserve fund, it would no longer be able to

meet the debt service requirements on the consolidated bonds.

You mean to tell me that the Commissioners could then affix their signatures to a certification saying that the Authority's ability to meet its commitments is not impaired?

The Witness: Your Honor, under those conditions, if my advice were asked, I would say they should not so certify.

The Court: They could not, could they? [618] If they had a set of figures in front of them, showing all of those circumstances, what happens?

The Witness: Your Honor, I would not think that they would so certify. I can't speak for what they would or would not do.

The Court: I am only asking for your opinion.

The Witness: In my opinion, they should not so certify under that hypothesis. T 593-8 to 618-11.

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[621] By Mr. Landis:

Q. One question, your Honor, does the Section 7 certification have to be made in connection with improvements and additions to a consolidated bond facility?

The Court: You mean existing facility?
Mr. Landis: Right.

A. Well, the answer to that is no. At Newark Airport, the redevelopment program, for example, your Honor, as you will recall, that there was at one time the possibility of building an additional airport in New Jersey which was not constructed and yet the additional capacity was needed. The State had made a determination it did not want that

capacity in that particular location and the airport at Newark was rather modest in size, as major airports go. Today, it is one of the most modern and efficient airports in the nation.

I believe that the expenditure of 400 million dollars with more to come has been made at Newark Airport since the time—that the redevelopment was initiated and that was made without certification under Section 7. T 620-3 to 620-25.

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[622] Q. If a subway rail system were constructed within the geographic boundaries of Newark Airport or if it suits, perhaps, if the same answer would be the same, the geographic boundaries of Newark Airport and the adjacent Port Elizabeth, Port Newark facilities, all of which are owned by the Port Authority or leased by the Port Authority under their control, and that railroad would cost 50 million dollars to construct and would lose 50 million dollars a year in net operating loss above revenues, would a Section 7 certification be necessary for the Port Authority to embark on a sale of bonds to pay for the 50 million dollar cost?

The Court: Are you saying would that constitute an addition to an existing facility or would that be an additional facility?

Mr. Landis: That's right.

The Court: Do you have an opinion as to that?

Mr. Sovern: It might be helpful to give the witness a copy of bond counsel's opinion, that a statute could not define a railroad to be an airport.

[623] Mr. Landis: I believe that it was a different set of facts.

Mr. Sovern: All right.

Excerpts from Testimony of Michael Zarin

Mr. Landis: I have no objection to getting into that, but I would prefer Mr. Sovern do it.

The Court: If you can answer that question, do you have an opinion?

The Witness: That is a difficult question because it is a question which has not only to do with the Commissioner or the Port Authority's judgment, there has been a legislative judgment that certain railroad facilities are in fact part of an airport, so that I am not so sure that counsel's opinion, Mr. Sovern, goes so much to the issue of Section 7, it goes to the issue of the 1962 covenant.

The Legislatures have, in effect, made the determination that at least certain railroad facilities by redefining the term airports, have made certain railroad facilities part of Newark Airport or part of Kennedy Airport, as I understand it.

That poses for the Commissioners and the [624] Authority a very difficult problem, mainly is this airport part of the facility or isn't it? The easy answer to the question is, it is part of the airport because the Legislatures have so determined it to be part of that airport.

As a matter of fact, when we were trying to build these airports, railroads and so forth within the covenant which we still are—I am sorry, I should not say that—at any rate, there was a theory that was propounded called the "adjunct" theory, which said that if the railroad was part of the airport, why could we not construct that facility and the Commissioner's easy answer, as I say, the definition of the airport now includes a railroad.

Therefore, the airport being an existing facility would not need to be certified in answer to your question.

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I think, myself, the question has a little bit more difficulty than that attached to it because in that event, what else could you add to the airport, but it is a question which we have not faced. In other words, [625] your Honor, if the World Trade Center had been defined to be part of the airport, could we then not have to certify the World Trade Center? I don't know, and that is why the theory is propounded as an adjunct theory, because at least this railroad would be going to and from the airport and some questions involved in that discussion ranged along the lines of if it was a railroad, just to the airport, would that be part of the airport or if you had commuter stops on it, would it not be, and so forth, even before the Legislature made that determination, but once they made the determination, I think your Honor will appreciate the difficulty of counsel advising that it is not part of the airport when the definition says it is, and what that advice would be, I don't know, because actually that problem was resolved in a different context which you will probably get into, namely whether it is part of an airport or an, it is still a railroad, and that I think is the opinion which Mr. Sovern was alluding to, namely that if it is a railroad, whether or not it [626] is part of the facility, there was a covenant protection for it. That is the way the analysis went. T 622-2 to 626-3.

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[630] The Court: If no one has thought of any more questions we will get to the covenant.

In what way does the covenant grant to the consolidated bondholders any greater protection than

they already had under the terms of the consolidated bond resolution and the Series Resolutions against the assumption by the Authority of a substantial deficit operation in the mass transit field? T 630-1 to 630-9.

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[631] The Witness: I believe that this morning, your Honor, we had commenced some discussion of this subject, and that we had been discussing the permitted purposes set forth in the covenant protection; the covenant providing that the resources, the revenues and so forth [632] of the Authority would not be pledged for any other purposes whatsoever other than permitted purposes, and we were discussing the permitted purposes under the mathematical deficit test. Your question—

The Court: As I understand Subsection 6—let's take the two aspects of the Subsection 6[b], the permitted purposes which are involved here. They could acquire, construct, operate a rail mass transit facility, if the Authority first certifies that the facility is self-supporting. Is that right?

The Witness: It could be approached from any particular way, and that is certainly a good way to approach it, the first or second—certainly if it is self-supporting.

The Court: That is right, if it is self-supporting. They include here a definition of what self-supporting means, that at the time of the certification the amount estimated for the ensuing ten years to be the average annual net income—which I guess is synonymous with the net revenues as that term is used in the consolidated bond resolution—derived from or incidental to such facility, equals or exceeds [633]

the amount estimated for such ten years to be the average annual debt service upon the bonds, presumably issued for purposes in connection with the facility. Is that right?

The Witness: That is correct. Essentially that is what we would call a one-times coverage.

The Court: One-times coverage.

The Witness: Right.

The Court: Now in order for the commissioners—I take it the commisioners must make the certification.

The Witness: Your Honor, in this case as distinguished from the previous case, the commissioners must make the certification. But I believe that the certification must also be signed by the governors. In the last sentence at the conclusion of Section 6 it says: Anything herein to the contrary notwithstanding any such certification by the Port Authority hereunder shall not be effective unless and until affirmatively concurred in in writing by the governors of the said two states.

The Court: Right. Now in order for the commissioners to make the certification I [634] assume that they would have to make projections.

The Witness: Subject to—I won't say the same thing to you I said to Mr. Landis. But subject to what I said to Mr. Landis the commissioners must certify it.

The Court: And they would have to have projections available to them of what the average net income would be and what the debt service requirements would be.

The Witness: Yes, your Honor, they would.

The Court: Isn't that the same thing they would have to have in front of them to make a Section 7 certification that we were talking about before?

The Witness: I think in regard to this section they would have to have something more than under Section 7's certifications for a couple of reasons: one reason being that this certification as distinguished from the Section 7 certification is not certification as to whether the Port Authority may meet that facility within the whole family of facilities.

In other words, there is a great deal more room for a range in that projection under [635] Section 7 than there is under this Section 6. As a commissioner you would need more precision to be able to get the answer to this subject. There are some other differences as well on that point.

The Court: I think I understand what you are saying. But in essence there must be projections made, so that the commissioners can make a determination whether they can certify.

The Witness: Your Honor, there must be projections; the bases of those projections are quite different one from the other.

The Court: I understand that. Now it was suggested I thought in some of the questions which were asked of you in connection with the Section 7 certification that it would be possible under Section 7 for the commissioners to indulge in a lot of latitude, but they were subject to pressures; and I think you were indicating that that would be a factor et cetera in making the certification.

The Witness: Your Honor, I made the statement that I was not able to judge what the commissioners

would take into consideration. And I am certainly not here to characterize the [636] actions of the commissioners of the Port Authority.

The Court: But presumably I can, if we assume that they are acting in good faith in both instances in making their certification. Is that right?

The Witness: Of course.

The Court: Then one would be really the equivalent of the others.

Let me go about it the other way.

If you want to attribute bad faith to the commissioners they could just as easily make a certification that a facility is self-supporting as they could that the Authority would be able to meet its financial commitments under Section 7.

The Witness: Your Honor, I am prepared to discuss the requirements of Section 6 and the requirements of Section 7. I am not prepared to discuss or characterize the commissioners of the Port Authority.

The Court: No.

The Witness: I could compare those sections and tell you I find certain differences and certain similarities. But as to the [637] commission's motivations I can't—

The Court: I grant you, we are not trying to go into—

The Witness: Furthermore I have some board meetings to attend after I leave this courtroom.

[638] The Court: No, all I am suggesting to you is this: that if one wants to assume that the commissioners would act in bad faith, which is an assumption that I would not make, moreover I'm not asking

you to make an assumption, other than for the purpose of this question, so if one wants to assume that they would act in bad faith they could make a certification as to whether a facility is self-supporting under this section just as easily as they could under Section 7.

The Witness: Your Honor, I respectfully differ with that statement. I'll be glad to explain why.

The Court: Please explain why.

The Witness: Your Honor, in order to explain this it would be helpful to utilize precise examples, and I don't know whether your Honor wishes to—

The Court: I don't want to get involved really in examples.

The Witness: All right. Then let me just read from the—let me just point out the portions of the statutes involved.

In a situation in which you are dealing with Section 7 under the consolidated bond resolution a commissioner would be permitted, [639] I would think, to rely upon understandings and projections with respect to his judgmental estimates of the future revenues of the Authority and that which he could reasonably assume would take place with regard to that facility and the entire family of Port Authority facilities.

On the other hand, when it comes to making up deficits with respect to the permitted deficits on Page 60 of my book, but I guess it's Section 6 under the definition of permitted deficits, you would not have to consider the amount of deficits as of the time of any certification hereunder for the payment of which one or both of the two states in connection with the proposed other railroad facility as to which the certification is made and in connection with the prior other railroad facilities has made adequate, secure and effective provision for the duration of the period for which the Port Authority is liable for such deficits.

Now, that means to me—

The Court: Doesn't that refer to the second half of it? That doesn't relate to a [640] self-supporting facility. That refers to a permitted deficit rail operation coming in under the second half of the permitted purposes.

We are still talking about a certification as to a facility being self-supporting. And they have a very exact definition of what self-supporting means, which you said was a one-to-one test. And on the assumption that this would be, let's say, a new facility, the commission will have to have the projections made.

And, granted, that they would not have the latitude that would be available to them in a Section 7 certification, because now you would only be focusing upon the operations of one specific facility. Nevertheless if you want to attribute bad faith to them they could either enlarge the projections or, let's say, be very liberal in their projections of the income and very restrictive in their projections of the expenses to show that it is self-supporting, couldn't they?

The Witness: Your Honor, I'm not assuming, of course, that anybody would be more than looking at the particular certification. [641] I don't know whether I read the statute precisely in that manner. I see in the statute taking them in progressive steps that your Honor is pointing to this one paragraph with respect to self-supporting as a certification. I would point out, as I have in that regard, that if you

wanted to make those projections you would in this particular statute have to make them with a much greater degree of care, first, because of the gubernatorial signature, which means that, I take it, that when a governor makes a certification he does not just sign his name also, but that it is there for the purpose that those certifications be subjected to a retest.

I would say to you as a person who has worked in government for a long time that when something is going to a governor it is treated with certain degree of great respect. So you would certainly not want anyone in the Governor's office, let alone the Governor, to be able to come back and say to you one thing or another about the certification.

That is not to say that the certifications under Section 7 would not be conducted with care, also. But if you want to talk about latitude [642] there is not that much latitude in this which there might be under that other one with relation to the asumptions which you make.

[643] The Court: All right.

The Witness: The second thing I woud say, and, of course, we are looking at some things through different eyes than we have to look our own in analyzing some of these things, but I would read this statute in a way under which a portion of these two tests, one self-supporting, and one deficits, are really two sides of the coin, namely if you found that there was a deficit, you could take care of that deficit in a particular manner under this statute either as I think we went into this this morning, a little bit out of the estimate of the general reserve fund or if there was an actual deficit.

The Court: I don't see how you can—maybe you can explain it further to me or maybe I am missing something, but as I read the statute, there are two types of permitted purposes with respect to the passenger rail transit. One is if the Authority certifies that the facility of that is self-supporting as hereinafter defined and the very next paragraph contains a definition [644] of self-supporting.

They were not involved with any question of deficits in that certification because by definition it has to be self-supporting.

Now, the other class of permitted purposes where you do have a deficit operation and just want to try to get over the first half, the first hurdle, and to contrast the kind of certification that you get there with the Section 7 certification.

The Witness: Your Honor, let us take an expenditure, a projected expenditure for operations on this railroad which is, let's say, the wages of the employees on this railroad and let us say that we estimate that the revenues under certain assumptions will be adequate to meet those projected wages and if in fact there is an increase in the fare over a certain period of time.

Now, as I understand what your Honor is asking me to opine, if in fact there was an inadequacy or a shortfall in that so that there were certain deficits, it was not self-supporting, that I might—and yet I am going to make that up in my judgment [645] with a—with a certain adequate, secure and effective provisions from the State, if there were a deficit and I could make it up with adequate safeguards—

The Court: We are not talking about deficits.

Excerpts from Testimony of Michael Zarin

The Witness: Your Honor, I am construing the same Section, we are dealing with the same Section and we are dealing with a statute which is providing for particular protections and I am just trying to understand how it is that a piece of an estimate which is not yet in hand in one part of this Section, namely the self-supporting section, should be treated differently from the protection which you would have to have if you had a dollar's worth of deficit.

In other words, this statute has within it the requirement, if there were a dollar of deficit and we were able to do this, that there be adequate, secure and effective protection or it be within the area of support and I cannot see why, at this moment, why in the self-support section, if we would just consider this generally, why that element of [646] revenues does not also need to be that sure.

The Court: All I am saying to you is that the Legislature that the Authority must certify that the facility is self-supporting. They have furnished us with a definition of self-supporting and in order to make that definition, one has to project the revenues.

The Witness: That's correct.

The Court: And the expenses, the debt service requirement, you fairly well know that that is not a problem.

Now, that is a projection of income and expense and all I am saying is that it is the same kind of projection of income and expense, I grant you, that there may be—you might have to be more exacting in making your projections, if you are acting in good faith.

The Witness: Because it is one facility.

Excerpts from Testimony of Michael Zarin

The Court: Because you are dealing with one facility rather than the whole panoply of facilities that the Port Authority has, still the certification is [647] based upon the projections.

The Witness: Without any doubts, it is based upon projections.

The Court: Now, you get to the second kind of permitted use and that is where you do have a deficit operation and perhaps you could explain to me how that operates in terms of how much of a deficit operation is permitted.

The Witness: A deficit operation is permitted under the permitted deficit definition and there it is stated, as I have indicated previously, that that deficit may be made up with adequate, secure and effective provision for the duration of the period for which the Port Authority is liable for such deficits is one way in which the deficits may be made up.

The Court: Now, let us go back to the beginning. At the very outset before you can go into a deficit operation, the general reserve fund must be full. Right?

The Witness: That is correct.

The Court: Okay.

The Witness: Well, I went directly to the permitted deficit definition, and [648] in going to the permitted purpose section.

The Court: You have to have your full reserve fund intact.

The Witness: That's right.

The Court: When the deficit of the new operation is combined, plus the PATH that was organized under Section C?

The Witness: That is correct.

Excerpts from Testimony of Michael Zarin

The Court: Cannot exceed the permitted deficits.

The Witness: That is correct.

The Court: Now, to get the permitted deficit, then we drop down to, first of all, the definition of a deficit. Right?

The Witness: That is right.

The Court: Now, what is your definition of a deficit, if you can give it to me without reading the paragraph?

The Witness: Well, the definition of the deficit is essentially the same definition as deficits. It is a definition which runs along the same lines as the definition of self-support which we discussed before.

It is a measure of income and outgo [649] and if the outgo over a ten-year period exceeds the income, you've got a deficit.

The Court: So again that is based on a projection?

The Witness: Again, it is based on an estimate by the Port Authority.

The Court: Now, the permitted deficit, supposing we went after that?

The Witness: That estimate, of course, also is—has a gubernatorial concurrence.

The Court: Yes.

The Witness: Well, now, there are essentially two methods of meeting that deficit.

The Court: A part is if you get the states—some kind of commitment that satisfies you?

The Witness: If there is adequate, secure and effective provisions.

The Court: That they are going to make up the deficit.

Excerpts from Testimony of Michael Zarin

The Witness: Right.

The Court: Now, we come to B.

The Witness: The B portion is essentially where we were this morning, namely [650] a measure of ten percent of the general reserve fund or an equity measure which essentially is measuring the same thing except that it is a testing situation in which the Port Authority has paid off a considerable amount of its obligations so the equity measure plus the ten percent of the general reserve fund would be a great amount of permitted deficits. We can go into that in some detail.

The Court: I do not think it is necesary. T 631-20 to 650-13. • • • So as I understand, if we go back to 1973 and take the Authority's financial statement or annual report for the year ending December 31, 1973, exhibit [III to the Stipulation], applying the B formula, the permitted deficit that would be authorized under B, could you show me how you calculate that?

I see it is ten percent of the general reserve.

The Witness: That's right, your Honor, [651] it is a moving decimal point calculation.

The Court: It does not include the consolidated reserve?

The Witness: That is correct.

The Court: Just the general?

The Witness: Just the general.

The Court: So you had 156 million dollars, approximately in the general reserve fund, right?

The Witness: If that is the amount, I am sure it is. This is the January 1 balance, your Honor. The balance of December 31, is 173 million.

The Court: Okay. So you have 173 million so you could have a permitted deficit of 17 million under that test.

The Witness: Approximately so, yes.

The Court: Applying the second part of the test, would you have a greater amount?

The Witness: No, your Honor, my understanding, and I am not testifying as an expert as far as the accounting is concerned, but my understanding is that the general reserve fund amounts to ten percent would give you the higher of the two.

[652] The Court: From what I understand, I think somewhere in the stipulation, the [loss] or the deficit from the PATH operation which must be included in the permitted deficit, right, exceeds the 17 million.

The Witness: Both statements are correct.

The Court: So therefore under the application of this formula, the Authority would be absolutely prevented in engaging in any rail transit operation.

The Witness: No, your Honor.

Mr. Sovern: Which is not—

The Witness: Which was not self-supporting.

The Court: Which is not self-supporting. T 650-16 to 652-17.

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The Witness: Your Honor, under the definitions, there are many railroad operations which could be self-supporting.

The Court: I realize.

[653] The Witness: Because we talked about adequate, safe, secure—

The Court: Are you suggesting that in the definition of self-supporting in the statute, the Authority

could take into account the state commitment?

The Witness: Yes, your Honor.

The Court: That would render them self-supporting?

The Witness: Yes, your Honor. T 652-23 to 653-11.

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[655] The Witness: Well, we have talked—that was the question, your Honor, that I understood you to be interested in, and the question, as I understood you to have addressed to me in which I considered since Monday night and we discussed most of the aspects of it, we discussed the exactness of this, of some of the mathematical computations of this distinction to Section 7 and we discussed the limit on 7, but we have not discussed at least from the standpoint of drawing the distinction, I think, your Honor probably has this in mind, is that in bringing an additional facility on line in the railroad area, we have under Section 7, the PATH railroad certified under Section 7 of the series resolution.

If we had done that and there had been no covenant protection under the statute, then we'd be in a position today of being able to add to the PATH railroad and take it to Plaintfield, say, as we are trying to do on a self-supporting basis [656] on the basis of an additional certification.

What this does in Section 6 is to say in paragraph "i" under purposes, that the permitted purposes include the Hudson Tubes as authorized and limited on the effective day of this covenant and the agreement. Then anything additional must be certified, as your Honor has very carefully pointed out when I went originally to the permitted deficit section

rather than staying with the permitted purposes exception for a longer period.

When you look at it that way, you see in some respects that it is really the heart of what it is that we are talking about.

We were able to undertake the PATH system, extend it 200 million or whatever it is on PATH, but we were not permitted to undertake additional operations, and your Honor knows that the deficits under the statute, as far as the Hudson Tubes are what we now call the PATH system is concerned, are not limited by the covenant. We may develop the PATH system and have [657] beyond, for example, the estimates which may have been before the Commisioners at the time of the PATH certification in the case of an additional railroad facility.

However, we might not go immediately on as, for example, we were able to do in the Newark Airport situation and that, in essence, is the covenant protection that we are talking about and I felt that without saying that to you, I would not have answered your question.

[658] The Court: All right. Well, couldn't the Authority then provide or, let's say, button up that loophole simply by amending the consolidated bond resolution or by changing the form of the series resolution?

The Witness: To do what?

The Court: So that a certification under Section 7 would be required whenever you are going to add to an existing facility.

The Witness: Could we increase the protections under Section 7?

The Court: Right. As I understand you, and unless I just didn't comprehend what you just said, you said that the covenant gives greater protection than existed under the series resolution Section 7 certification because once having acquired PATH without the covenant you would then not have to issue any Section 7 certification to extend the PATH operation. But with the covenant now you must make certification. T 655-2 to 658-22.

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[661] All right, do you have any other reasons for your statement that the covenant [grants] greater protection than what the bondholders had before?

Now, for example, I assume that the covenant does not give the bondholders any protection at all against the Port Authority's assuming other massive deficit facilities [662] other [than] rail transit.

The Witness: As far as that's concerned, your Honor, the covenant only applies to railroads. And that really is an example of response, as I've looked at it, that was made to the problem that was presented at that time. We, for example, as we just discussed in connection with the ability to free the consolidated bond reserve fund a little more, we were able to do that. In essence, these covenants, and I've negotiated some of them, are exactly that, a process of negotiation, and even within the covenant itself if it was opened up actually—actually today I don't think it's significantly greater. It would be if—if the original projections were true for example. I don't mean that they weren't, held true. If the original protections had held true with respect to PATH, that is to say that the fares had been increased as we went

along and we were still at the 5 million or 6 million dollar figure we would now have an ability to put $12 million per year into those deficits, but I think [663] your Honor is quite right that just addresses this particular problem and it doesn't address the problem, for example, that that Goldberg speech did of taking the school system into the Port Authority.

[664] The Court: Or a second World Trade Center, or let's say the hospitals of the City of New York. These are all deficit operations which somebody would like to pass off on to you.

The Witness: That is true, your Honor. This responded only to the one that was in the public eye at the time and not to others. . . . T 661-19 to 664-8.

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[674] [By Mr. Landis] Q. Would it be fair to state that the certification required under the 1962 covenant is a certification of an amount?

The Court: Certification?

Mr. Landis: Of an amount.

The Court: Which one?

Mr. Landis: The certification under the 1962 covenant.

The Court: But there are different kinds, self-supporting—

Mr. Landis: Whether it is self-supporting or deficit, I don't think in the context of the question it matters.

The Court: You say certification of an amount.

Mr. Landis: Yes, I am asking if that is a correct characterization of the certification.

A. I don't know, Mr. Landis, whether it is the certification of an amount in the sense that the amount itself would have to be spread on the certification. In order to make the certification you would have to [675] have materials, and certainly which would reveal that amount. I have not myself gone through the process of preparing—as Mr. Sovern indicated, I have not prepared such a certification for a facility. So I am certain it hasn't been done as yet under this particular statute.

In order to make the certification, if you were making it or if you were concurring in it, you would of course have to have documents which would show amounts. But whether the certification itself would say that you want to certify that this complies with Section so-and-so, and so forth, and that would be signed, or whether it would spread forth the entire economic analysis, I don't know at this point.

Q. It would be necessary to come to certain conclusions as to amounts, would it not? A. Yes, sir.

Q. Would it be fair to state that the certification required under section 7 would be the certification of an opinion?

Mr. Sovern: I think I will object, your Honor, the covenant is explicit and you examined at considerable length on this subject.

The Court: Yes. He apparently has never had to cross that bridge yet. That is what he is telling you.

[676] Mr. Landis: I am not sure what the answer is, but I am simply trying to get a characterization of what may appear on the record as a rather confusing discussion.

Mr. Sovern: I will withdraw my objection. The text of the resolution says it shall certify its opinion.

The Court: The text of—

Excerpts from Testimony of Michael Zarin

Mr. Sovern: —of the resolution about which Mr. Landis inquired. Section 7. He asked whether the consolidated bond resolution the series resolution, Section 7, called for a certification of an opinion. I objected. I looked at it. I saw it does. I withdrew the objection.

The Witness: You are speaking now of the series resolution itself?

Mr. Landis: Yes, the Section 7 of the series.

The Witness: Mr. Sovern has read it.

Q. Do you subscribe to his answer? A. It says: If the Authority shall certify at the time of issuance its opinion. T 674-5 to 676-23.

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[684] [By Mr. Sovern] Q. • • • Mr. Zarin, tell me again why you regarded little "i" of permitted purposes as an important limitation? The Port Authority has in fact improved the facilities on the line and I thought you testified that had it been but for little "i", the PATH could have grown like Newark Airport, you would have added more. A. If I gave you that assumption, I'm just saying to you that little "i" delimited a particular system and took the PATH system as one—for example, let's assume that we started with your railroad, that you are talking [685] about B and that was little "i". We could have improved that railroad as much as we wanted to.

Q. Stay with PATH, if you would, please. You said little i was very important. Those weren't your exact words, but that was your message.

Now, what is its importance? A. The importance is under little i, you can improve PATH as a system as far as PATH is concerned.

Excerpts from Testimony of Michael Zarin

In contradistinction—and then taking the covenant protection, let's assume, if I may, and stop me if I am going out of your hypothetical, staying with PATH, you asked me to assume the covenant protections. Let's for a moment assume only section 7 with respect to little i.

Q. I'd really rather not.

The Court: Just stick with PATH, and the question, is really, what does little i mean?

A. Little i means that just as you can build a railroad across the George Washington Bridge without reference to the covenant, you may acquire and improve the PATH system without reference to the covenant.

The Court: But you could not add trackage to PATH, extended to—

The Witness: Your Honor, that is [686] precisely so, that is the nub of the—

Q. When you said little i was the nub of the covenant, what did you mean? A. I really am trying to explain that, and what I meant was the question to which I was really responding was really all through this thing, is what is the difference, what is the added protection of the covenant and little i illustrates the difference between PATH and say, Newark Airport in the examples I have given today.

In the case of Newark Airport, we were able to extend the Airport by agreements and it is in different locations and so on and so forth.

Q. If it were not for little i, you could have done that with PATH? A. If it were not for little i we could have done with PATH, right.

Q. That is what I thought you said, if you could have done that for PATH. A. Not if it were not for little i, I

beg your pardon. With little i we could do it for PATH. If it were not for the covenant, we could extend PATH as far as—let us put it this way, section 7 would not have to be put into play again with respect to little i as a facility, a railroad facility.

Q. If you want to tell me section i is [687] unimportant, I would take that, but I do not think you could have meant to say that it is the heart of the covenant in that it authorized the greater expenditures on the H&M because if you recall the Judge had just asked you an open-ended question, what else did the covenant do to protect bondholders that the other things didn't and as you did with me and I assume Mr. Landis, pointed out that little i limits the extent to which the H&M can grow. A. Mr. Sovern, I don't believe that I specifically referred in our conversation to little i. I believe that my first reference to that was here on the stand.

Q. You are quite right. A. Thank you.

Q. I withdraw that reference. I was just collapsing a lot of stuff together. A. What I was intending to say, and I have been very careful today, it is starting to get late, and when I said the heart of the matter, there are so many things that I could have characterized that way, and I am sorry I said the heart of the matter. It demonstrates to me the difference of PATH and the Hudson Tubes by putting it into the exceptions and saying it is not subject to the covenant, makes PATH the same kind of thing as other facilities except for one fact, and that is in order to [688] prevent it from being considered the same as those facilities, it says not PATH but—or Hudson Tubes, which is virtually synonymous. It says as authorized and limited on the effective date of this covenant and agreement.

Newark Airport on the other hand, does not say Newark Airport as authorized and limited on the effective date of

this covenant and agreement, so that settled PATH in one section and then if you wanted to do anything additional, you have to name it and certify it. Once you named it and certified it, if it meets all of those tests, then it too becomes part of the family but if you want to add to it you have to certify more to that.

Now, if that is not the heart of the matter, it has—maybe it is not and it has some importance.

Q. The paragraph at the end of the covenant says in the third sentence, "Each certification by the Port Authority hereunder shall be made at the time of the issuance of its first bonds," et cetera.

Now, I would suppose that that applies to PATH.

A. No, sir, it says, "In connection with a proposed other railroad facility," is what I have been trying to point to permitted purposes for.

Any other railroad facility. I assume this has nothing to do with PATH.

[689] Q. I wasn't fully—precise. I would assume it would apply to an effort to extend PATH beyond its present boundaries? A. Yes.

[690] Q. All right. So that paragraph, if you read it that way, would require a fresh certification if PATH was sought to be extended beyond its present boundaries. A. Precisely so.

Q. What does a little "i" do for the bondholders? A. Oh, little "i" doesn't help the bondholders. Little "i" is what we got.

Q. Okay, fine. I think I— A. We got— we got that. We got that. We got the ability to put all that money into this system. That's what this whole statute was about. T 684-16 to 690-13.

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Excerpts from Testimony of Michael Zarin

[711] Q. I take it there is no question, is there, Mr. Zarin, the bonds in the 40 and 41st series do not have the covenant in their contract? A. They do not have the covenant in their contract with respect to those obligations, right. I think the official statement—

The Court: That is your answer, that is sufficient.

Q. Now, second, I don't want to go into a long list, but you had not finished your answer— A. Well, your Honor, the official statement is put together in very careful terms with respect to the 40th and 41st series of bonds and states on page 17 in the statutory covenant against dilution of pledged revenues and reserves by additional passenger railroad facilities, remains in effect with respect to affected bonds and remains binding on the Authority, although it does not apply to the bonds of the present offering. T 711-2 to 711-19.

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Excerpts from Testimony of Austin F. Fitzgerald

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[721] AUSTIN F. FITZGERALD, 53 Central Avenue, Glen Rock, New Jersey, sworn.

Direct Examination By Mr. Landis:

Q. By whom are you employed and in what capacity, Mr. Fitzgerald? A. I'm employed by Weeden & Company, and at the present time I'm vice-president in charge of dollar bond deposits and I am also in charge of the corporate bond trading department, and have the responsibility for our activities in the long government bond area.

Q. What is your educational background? A. I'm a graduate of Saint Peter's College in Jersey City where I received a Bachelor of Arts degree with a pre-med major. I have also taken courses in NYU Graduate School of Business Administration.

Q. How long have you worked in the area of municipal bonds? A. For approximately 20 years.

I came out of service in 1954, joined James H. Olyphant & Company, became a registered representative.

I think I then switched to the firm of [722] Meaney and joined Weeden & Company in 1957.

Q. What did you do when you first joined Weeden? A. At that time, I was in the stock area of the firm.

I then moved into the municipal dollar bond trading area. From 1958 to 1962 I worked with another fellow in the department.

At that time I became responsible for running the department, and by 1970 I was responsible to, allowed by the firm to commit up to 30 million during any one trading day.

In August of 1973 I also assumed my additional responsibilities in the corporate and government area.

Excerpts from Testimony of Austin F. Fitzgerald

Q. Were you what is commonly known as a trader during that period of time? A. Yes. At this time I was a trader, which meant I would purchase and sell bonds for the benefit of the firm's account.

Q. At the present time what are your responsibilities? A. All right. At the present time I actively supervise the trading of bonds. Previously I was actively engaged each day in terms of the trading [723] responsibilities. At this time I now have the overall supervision of the dollar bond trading department as well as the corporate trading and our government activities.

In this I will confer with Allen Weeden, to whom I am directly responsible, as the president of the company.

Q. And what is the involvement of Weeden and the scope of that involvement in the municipal bond area? A. In terms of this Weeden is a major dealer, in terms of underwriting of securities, we also are participants in the secondary market and are major market makers in terms of this. Weeden itself has approximately 500 employees.

We have eight offices, which are located in San Francisco, Los Angeles, Chicago, Philadelphia, Boston, New York and London.

Of our business, it's broken approximately into the bond business is approximately 60 percent in the municipal bond area, 40 percent in the corporate and government area. Of our business in the municipal area two-thirds of this is done in the secondary market. We will take a position in a dollar bond area of, as I had said earlier, [724] of approximately as high as 30 million.

We would have transactions in Port of New York Authority bonds one given day, probably in the area of four to six hundred thousand.

Excerpts from Testimony of Austin F. Fitzgerald

We also would do business in the dollar bond area of between approximately two to three million in purchases and sales. Our total business in the firm for the year would come to approximately 25 billion.

[725] Q. Has Weeden been involved in underwriting Port Bonds? A. Yes, we have. We have been a major in the underwritings of most of the Port issues.

We also have been managers of several of the competitive bidding deals and the ones that we have not been involved in, those where we were lost out in the competitive.

Q. How many different issuers of bonds are you familiar with? A. Approximately one hundred.

Q. That is on a personal basis? A. Yes.

Q. And what kind of clients does your firm deal with? A. We deal primarily with institutions and dealers. Institutions would be composed of such as banks, insurance companies, public and private pension plans, municipalities, trusts, etc.

Q. And are the dealings of Weeden in the Revenue Bonds on a national basis? A. Yes, [they are].

Q. Is that true also of deals specifically with Port of New York Bonds? A. Yes, it would be.

[726] Q. Who are the major dollar bond dealers in the business today? A. The major ones would be Salomon Brothers, Barr Brothers, Merrill Lynch, Park Ryan, and ourselves.

Q. Specifically with reference to the dollar bonds that we are involved with here in this litigation, the Port Authority Bonds, who are the major dealers in those bonds? A. It would be Barr Brothers and ourselves.

Q. How long has your firm been making a market in dealing in Port Bonds? A. I guess about 25 years.

Excerpts from Testimony of Austin F. Fitzgerald

Q. Do you consider yourself to be familiar with the secondary market of Consolidated Bonds of the Port Authority? A. Yes, I would.

Q. How do you base that judgment, what do you base that judgment on?

The Court: On everything he has just told me.

Mr. Landis: Fine. I would then offer him as an expert dealer.

The Court: Any questions with respect to his qualifications as an expert?

Mr. Sovern: No questions. We accept [727] him as a expert.

Q. You are aware, are you not, Mr. Fitzgerald, of the subject matter of this litigation? A. Yes.

Q. And you have heard of the 1962 covenant? A. Yes, I have.

Q. What is your general understanding of what that means? A. Generally, it was considered as a security for the bondholders and it protected the diversion of the earnings of the Port Authority into deficit mass rail transit.

Q. What effect did the legislation repealing the covenant have on your attitude and your firm's attitude towards Port bonds? A. A very negative effect in terms of that. It greatly restricted the amount of money we were willing to commit to the secondary and primary market. As soon as we became aware of the possibility of the repeal.

I might add, that we were undoubtedly not alone in terms of this feeling. In other words, the feeling of the community was—we could determine that they were less willing to make commitments in terms of this and this had a great effect in the market in terms of the fact that the market was no longer as viable a market [728] as it had been prior to the repeal of the covenant.

Excerpts from Testimony of Austin F. Fitzgerald

Q. Since the repeal, has Weeden continued to make a market in Ports? A. Yes, we have continued to make a market and we will continue to make a market. However, we no longer do it to the degree, nor commit the capital that we would have prior to this, and in addition as to not being willing to commit the same amount of money, we also wish to receive a greater margin of profit in terms of the amount that we commit. In other words, the risk has increased, so therefore the profitability should.

Q. In general, how would you describe the market for the Port bonds since the repeal of the covenant? A. Very thin and very sensitive. T 721-2 to 728-15.

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Q. Do you still deal with any investors? A. Yes.

[729] Q. Would you explain that? A. Yes. While I no longer have the day-to-day responsibility, or while I have the responsiblity I no longer conduct the activities myself. There are still people with whom I will talk and discuss things in this manner.

Q. What effect did the repeal have on the attitude of those people? A. They no longer will either buy the bonds outright, nor will they buy them on swaps. This is true of customers such as Banker's Trust, United States Trust, Connecticut General, Fireman's Fund, First National Bank of Chicago, First National Bank of Louisville, and St. Louis Union.

Q. What effect, then, do you see that the repeal has had on the market for Port bonds? A. Basically it has had a very negative effect, and the repeal of the covenant has caused the bonds to decline to a much greater degree than other comparable bonds during this period of time. It also has—

Mr. Sovern: Excuse me. Would you say what period of time, please?

The Witness: The period of time of the repeal.

Mr. Sovern: Down to today?

[730] The Witness: Excuse me?

Mr. Sovern: Down to today's date? Yesterday's? What is the cutoff period that you are referring to when you say during this period of time?

Mr. Landis: May I object to cross-examination during the midst of his answer.

Mr. Sovern: It is not cross-examination. I was objecting to the question as insufficiently clear, if you would prefer that I do it that way.

Mr. Landis: I think you should object before he starts to answer the question rather than after he starts to answer the question.

The Court: I think Mr. Sovern was asking the witness that just for purposes of continuity. I think it would be proper to specify what period of time you are talking about. You say since the repeal to date?

The Witness: Yes.

The Court: The decline has proven greater in comparable bonds?

The Witness: That is true. Although when you say today, there has been an improvement in the market in the bonds.

The Court: In Port Authority's [731] particularly or in all bonds?

The Witness: In all bonds. However, the improvement in the Port Authority bonds has been greater recently than the improvement in some of the other bonds.

The Court: When you say recently, could you indicate approximately when, for Mr. Sovern's purposes, that improvement began? You do not have to give an exact date, but just generally a period of time.

The Witness: I would say approximately in the middle of January, the first week in January.

By Mr. Landis:

Q. Do you have an opinion as to the result— A. Yes, in terms of this: that this has caused this negative effect, and if the repeal in our opinion, if the repeal does not take place, the covenant is still allowed to stand that this will then continue into the future. In other words, if the covenant is not repealed we will see a further decline in terms of the price of the Port of New York Authority bonds. T 728-22 to 731-22.

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[732] Q. Would you explain what your opinion actually is? A. Basically it is that obviously the covenant was repealed. So unless the covenant is reinstated, we will continue to see the same type of thing that takes place in terms of the price of the bonds.

Q. You mean—A. A decline in relationship comparable to the bonds. T 732-9 to 732-16.

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[734] *Cross-Examinaton By Mr. Sovern:*

Q. Mr. Fitzgerald, you testified that there were certain movements in the price of Port Authority bonds from sometime around repeal down to date. Is that correct? A. That is correct.

Excerpts from Testimony of Austin F. Fitzgerald

Q. Relative to other bonds and the Port's themselves. Would it be accurate to say that some portion of the change in the prices of Port Authority bonds during this period was attributable to a technical situation? A. From the repeal to the present time?

Q. That is right. A. In my opinion that would probably be true.

[735] Q. A short-term technical situation? A. To answer in terms of short-term is a—

The Court: You want to know what he means by short-term?

The Witness: That would be helpful.

The Court: Is that a term used in the security industry and municipal bond industry, a short-term technical situation?

The Witness: Yes.

Q. Okay. What does it mean? A. Okay. Basically when people refer to short-term, they mean over a period of time which they will anticipate will be two, three days, a week, two weeks, three weeks.

Q. Three weeks? A. But it could—this is what I was going to say in terms of this: When you get into the idea of short-term technical there are times when short-term technical situations can last for a longer period of time, and you could have—short-term, there is no definite period of time when people will pick to say, that's short-term when they do things such as this, you know.

Q. But normally it would be from anywhere from two to three days to three weeks? [736] A. Well, it could last for two months.

Q. Could it last for nine months? A. No.

Excerpts from Testimony of Austin F. Fitzgerald

The Court: In the bond market that would be a long-term phenomenon, nine months, if something happened it would be considered long-term?

The Witness: In the trading aspect of it, your Honor. It obviously wouldn't be in terms of an investment approach. T 734-3 to 736-11.

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[737] Q. So the price decline about which you [738] were speaking is roughly from May, early May, mid May, late May [1974]? Can you be more precise? A. It's pretty hard to be.

Q. All right. Sometime in May until the first week of February [1975].

Now, during that period, put it this way, did anything occur during that period other than repeal of the covenant that might, in your opinion, have affected the price of Port Authority bonds? A. Nothing as it would be say opposed to you know, the general market area, in other words, the general level of interest rates.

Q. Because a general decline would have affected the prices, repeal would have affected the prices, what else, if anything, can you think of that would have affected the prices? A. Offhand, I—you know, in terms of specifics, I can't really think of anything.

Q. Are you familiar with the basic financial condition of the Port Authority insofar as publicly reported? A. Yes, although I couldn't claim to be an analyst, or anything in that respect.

Q. Are you aware of anything that has [739] happened, any reports of its financial condition that came out during the period between May and the present that might have affected the price of Ports? A. In what sense?

Excerpts from Testimony of Austin F. Fitzgerald

Q. Well, do you recall seeing the [reports] of the World Trade Center being in difficulty? A. I may have in terms of that, but in terms of that, people have been aware for some time.

Q. That the World Trade Center is in difficulty? A. No, I wouldn't use the word "difficulty," but in terms of the fact that they are attempting to rent their space. Office building rental space in New York isn't what it used to be.

[740] Q. Has that market gotten better or worse in the last seven or eight months? A. Gee, there, again, frankly, I couldn't tell you the answer to that. I don't know. T 737-25 to 740-5.

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Q. That [S-1] is a *Wall Street Journal* story, you see that came out during the month of August. Could that have an effect on bondholder enthusiasm in Ports? A. Do you mind if I finish reading it?

Q. No, not at all.

Do you think, Mr. Fitzgerald, that that might have had an effect on bondholder acceptance of Ports? A. I don't believe that it would have in terms of this article.

Q. And that is because you think—well, why do you think that? A. All right. I believe that it was known by [741] people at that time that this was approximately the level of the rental of space in the World Trade Center.

Q. Have you seen this story before? A. I don't believe that I have seen this specific one.

Q. Counsel provided us with some documents.

Were they your personal documents or the firm's documents? A. They were the firm's documents, yes.

Q. There may be material in that file that you have not seen? A. That's quite possible.

Excerpts from Testimony of Austin F. Fitzgerald

Q. I want you to show you now an Exhibit marked as S-2 from the *New York Times*—I am sorry, November 10, 1974, and I can now tell your Honor that it was on the front page of that [edition] of the TIMES headed, "Port Authority has fallen on hard times" T 740-13 to 741-21.

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[742] Q. I would ask the witness to examine, as well, P-89, and the question—and please feel free to take as much time as you need, Mr. Fitzgerald, do you think the *New York Times* story, S-2, in evidence, had an effect on the price of Port Authority bonds? A. May I finish reading it before I answer the question?

Q. Yes.

Now, you have read S-2. Have you had a chance to look at P-89? A. Yes.

Q. The question is do you think the Sunday [743] *Times* story of November 10, 1974, may have had an impact on the price of Port Authority bonds? A. In my opinion, it would not have had an impact to that great a degree, this story.

The Court: Keep your voice up.

The Witness: No, I don't believe it would have had an impact to that great a degree. I believe that most people who were owners of bonds would have probably have known in terms of the facts that are contained in this story. • • •

[By Mr. Sovern]: . . . Some Bondholders would not, though. Is that correct?

The Witness: It's possible. T 742-13 to 743-24.

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[744] Q. As you look at P-89 and you see a price of Port bonds dropping like a shot right after this story appeared in the Sunday *Times*, can you explain that drop by any other event? A. I would, to my mind, the way I would characterize it in terms of this, is that it is a continuation

of what had been going on before. In other words, I could not say that it would be due to the story in the *Times*, as well as it would be due to the earlier decline that took place prior to this story.

Q. So you think that the drop in the chart reflected immediately after November 10 is just a delayed reaction to the repeal? A. I wouldn't—I don't believe that the true answer can come out in that manner in the sense that if you have a negative reaction to news, this will take place, but the length of time that it will take it to take place, no one can really tell that, it will be an ongoing thing.

Q. Did you notice any pattern on selling immediately after the repeal? Was there heavy selling? [745] A. There was a reasonable amount of selling, but once again, to explain this, you are not dealing with an auctionable market. You are dealing with a market where people are bidding and asking for their own account and therefore you would have to, to have had the selling, you would have to have people who are willing to stand up and buy bonds as well as the sellers, and the market has been characterized by the fact that it is a thin market, as we have indicated.

[746] Q. Has it always been thin? A. What?

Q. Has the market in Ports always been thin? A. No.

Q. When did it become thin? A. You could say probably it started last April, May.

Q. And it has remained thin ever since? A. Relative to what it had been prior to that.

Q. You said that you had heard of the covenant and it was generally considered as security for bondholders in that it prevented the diversion of Port Authority earnings to mass rail transit. Is that correct? A. That is correct.

Q. Are you familiar with the terms of the covenant? A. In a general manner.

Q. Do you advise people about its meaning? A. No. We are not in the advisory business.

Q. How long have you known that it covered rail transit? A. Since 1962.

Q. Did you read it at that time? A. As a covenant in terms of reading through the [747] entire thing? I glanced at it in terms of that.

Q. Have you discussed your testimony in this case with anyone? A. Yes.

Q. With whom? A. With the counsel for the United States Trust.

Q. I think you have testified you committed less capital to Ports when you became aware of the possibility of repeal. We have referred to that before. Are your inventories in municipals of all kinds? Heavier or lighter today than they were in 1973? A. You will have to give me time to think back and reflect a little on this.

Q. Please. If the date is troublesome, take it back to 1972.

Let me make it easier for you. At least I will try to make it easier. Have your inventories become lighter generally lately? A. I could be facetious either way about that.

Q. Answer whichever question you find you want to do.

Mr. Landis: Maybe he can t find either.

A. In general I would say they would be probably lower, but not to a great degree. In other words—

Q. Generally lower, then, is your answer. [748] A. Yes, that is in this specific area.

Q. Municipal bonds. A. Municipal dollar bonds.

Q. Municipal dollar bonds. A. Yes. T 744-4 to 748-5.

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[752] Q. Are municipal bonds regarded as secure investments, Grade A? A. Most of them are.

Excerpts from Testimony of Austin F. Fitzgerald

Q. So that a high quality municipal bond has advantages of both the tax-free yield and high security. Is that right? A. Would you repeat the question, please?

Q. A high-grade municipal bond has the advantages both of a tax-free yield and high security. A. Yes. T 752-11 to 752-20.

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Excerpts from Testimony of Gordon Fowler

[761] GORDON BLACKFORD FOWLER, 21 Cliffmore Road, West Hartford, Connecticut, sworn.

Direct Examination By Mr. Landis:

Q. By whom are you employed, Mr. Fowler? A. I am an employee of the Connecticut General Life Insurance Company located in Bloomfield, Connecticut.

Q. What is your capacity? A. I am a secretary in the bond department, responsible for public debt investments.

Q. And what is your educational background commencing with your college education? A. I have an A.B. Degree from Princeton University and an M.S. degree from Columbia University School of Business.

Q. In what areas of study? A. Business administration and in economics at Princeton.

Q. Where have you employed since your education? A. Following Columbia, I went to work for Connecticut Mutual Life Insurance Company in [762] Hartford, Connecticut, in a non-investment capacity.

The following year, I changed employment and went to work for Aetna Insurance Company, located at 55 Elm Street in Hartford.

In 1962, Aetna was acquired by the Connecticut General Life Insurance Company and in 1964, the Aetna's investment department was merged into that of Connecticut General's.

At that time, I came on the payroll of Connecticut General Life Insurance Company and I worked there ever since.

Q. What did you do at Aetna and since Aetna was merged into Connecticut General at Connecticut General. A. While I was at Aetna I was in municipal bonds, as

an analyst, and on joining Connecticut General, I became a senior analyst responsible for municipal bonds.

Q. When you say municipal bonds, what did that entail? A. Well, that at the time involved reviewing new bond issues and making recommendations for purchases and sale of such securities.

Subsequently, I became an officer of [763] Connecticut General in 1968. At that time, I became responsible for making the decisions and executing purchases and sales of those bonds.

Q. When did you attain your present capacity? A. In 1972, I became a secretary of the corporation.

Q. What are your responsibilities in that capacity? A. I am responsible for public fixed-income securities. This includes corporate bonds, municipal bonds, U.S. governments and its agencies; the total amount would be about a billion one, under my supervision, of which 500 million are municipals—500 million are corporates and 100 million governments.

Q. Does Connecticut General or Aetna presently own any Port Authority bonds? A. Yes, we do.

Q. When were those purchases made? A. The initial purchases of bonds we hold now were made in 1968.

At that time, we purchased 875,000. Each year since then to 1973, we added to those holdings and at the end of 1973 we held a total in all [764] companies of $9,450,000.

Q. Were those purchases made in the secondary market or upon original issue? A. With the exception of 3 million 40th series bonds, substantially all were made in the secondary market.

Q. In your purchases between 1968 and 1973 in the secondary market, were you aware of the existence of the 1962 covenant? A. Yes, I was.

Q. Did the existence of the covenant affect your decision to purchase those bonds? A. I relied on it at the time I purchased the bonds, yes.

Q. Now, with respect to the 1973 purchase of bonds, did you purchase those bonds with knowledge of the 1973 prospective repeal of the 1962 covenant? A. Yes, I did.

Q. Would you explain that decision? A. Well, the 40th series bonds which we purchased were not covered by the covenant. However, of approximately a billion seven, thereabouts, of outstanding Port Authority bonds, were protected by the covenant and it to me was [765] unreasonable to expect that these bonds would be fully retired in the immediate future or even the forseeable future and therefore the 40th series bonds were indirectly protected by the covenant.

Q. With respect to all the purchases you described, would you have purchased any of those bonds without the protection of the covenant? A. I can't say for certain we would not have purchased them, but if we had, it would have been at a much lower price for the given coupons.

Q. Since the 1974 repeal of the covenant, have you purchased any other Port Authority bonds? A. No, we have not.

Q. Did you take action with regard to the bonds that you held? A. We sold two million of our 40th series bonds at cost in the first part of 1974.

Q. Why did you decide to sell these bonds at that time? A. The likelihood of the repeal being effective—not being effective, but occuring, was of concern to us.

Q. What would that entail in regard to those bonds? [766] A. Well, we were concerned with respect to our entire holdings, that if the repeal were effective, that the earnings of the Authority will be diluted by additional passenger rail facilities.

Excerpts from Testimony of Gordon Fowler

Q. Did you try to sell any other bonds of the Port Authority at or since that time? A. No, we have not. We have principally tried to sell those 40th series bonds. Had we had an opportunity to sell bonds without incurring a substantial loss, we would have been favorably inclined to do so, however.

Q. Did you try to sell the bonds of the 40th series, that you still hold? A. Yes, we did. We tried to sell the remaining one million.

Q. I gather you were not able to? A. No, we were not.

Q. Why was that? A. The price of the bonds had deteriorated to such a low level that we were unwilling to take the loss if we were required to sell them.

Q. I gather then you continue to hold substantial amounts of Port Authority bonds. A. That's correct, we still hold $7,450,000 [767] worth.

Q. What is the reason, justification, for continuing to hold those bonds, if there is one? A. Well, we are optimistic, but the repeal will not be substantiated or the Court will not allow the repeal to become effective and we are unwilling at this time to take the loss if we were required to sell the bonds.

Q. Since the 1974 repeal of the covenant, have you purchased any moral obligation bonds? In the State of New York, or New Jersey and their agencies or subdivisions? A. No, we have not.

Q. What is the reason for that? A. It is the general feeling that if the Legislature of the two states would renege on their obligations with respect to the Port Authority covenant, we have no reason to believe that they would live up to the moral obligation, which is not a legal obligation. T 761-3 to 767-22.

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Excerpts from Testimony of Gordon Fowler

[769] Cross-Examination by Mr. Laulicht

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Q. Now, as I read S-26, in 1971, Aetna purchased a net total of $2,150,000 worth of Port Authority bonds. Is that correct? A. No, let's see—we held—you are talking about 1971?

Q. Yes. A. We owned a million eight at the beginning of the year and we had two million nine—okay, two million nine hundred fifty. The difference there is two million one hundred fifty thousand.

Q. Now, in making your decisions—and I take it you were responsible for the decision to buy that $2 million worth? A. That's correct.

Q. In making those decisions, did you rely on research reports that were in the files of Connecticut General? A. We principally relied on the official statements. We do get various research reports and the time—I [770] don't have a specific recollection of relying on it directly.

Q. Well, if a research report comes in from Hornblower and Weeks, that would come in to your office would it not, Mr. Fowler? A. Yes, it would.

Q. Would you normally read it? A. Generally, yes.

Mr. Laulicht: I would like to offer as S-27, a document which has been marked originally as P-102. I take it this comes from the files of Connecticut General. It does come from the files of Connecticut General, according to Plaintiff's Counsel.

Is that the type of report.

Mr. Landis: I object to it.

The Court: Let him ask the question first.

Q. Is that the type of report that would come to your office? A. Yes, it would come either to myself or my associate who works with me on municipals. T 769-7 to 770-22.

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Excerpts from Testimony of Gordon Fowler

[775] Q. Did you or have you read Dun & Bradstreet Reports about the Port Authority? A. Pretty much as in the same fashion as this Hornblower Report. I have looked at them from time to time, but have no specific recollection of any given report.

Q. Mr. Fowler, in making your decisions with respect to what bonds to buy, do you rely on anything other than the official statements relating to those bonds? A. We principally rely on those.

[776] Q. Yes, and what else do you rely on? A. Well, obviously to the extent those reports are available we look at them at the time.

Q. Anything else? A. Well, I would say those are the major things.

The Court: You have an astrologer, or something?

The Witness: No.

There is, of course—there is the oral-type communication an investment banker might convey.

Q. Do you know anything about the rating system that Dun & Bradstreet used to employ? A. Not a whole lot, no.

[777] Q. Do you know what a rating of 0-7 would have meant for Dun & Bradstreet in February of 1972? A. My recollection was that that was a fairly respectable rating, but until Dun & Bradstreet took over Moody's, I really have not relied on Dun & Bradstreet type ratings. Even now I don't rely on Moody ratings.

The Court: How about S & P?

The Witness: S & P, I don't rely on them. We do our own analysis, but I would possibly give S & P a slightly better score at this point.

Excerpts from Testimony of Gordon Fowler

The Court: But you rely principally upon your own analytical work?

The Witness: That's correct.

The Court: In making your investment decisions?

The Witness: That's correct.

The Court: Plus such information you get from members of the investment banking community in whom you have confidence?

The Witness: That's right.

By Mr. Laulicht:

Q. Now, in light of your statement that [778] you just made that you don't rely on Moody's, but you could rely on Standard & Poor's— A. I'm sorry but I didn't say that.

The Court: He didn't say that. He just said he would give S & P a better rating than Moody's. That's all.

Q. I'm sorry for misstating it, but in light of what you just said can you explain to me how it is that you have at least two Moody's reports with respect to the 40th and 41st series according to the exhibit list, and you don't have a Standard & Poor's report. A. That's because we subscribe to a service put out by Moody's Investors Service, and I'm unaware of any similar service at Dun & Bradstreet.

Q. Well, Dun & Bradstreet is not my question. My question relates to Standard & Poor's. A. I don't mean Dun & Bradstreet, I mean Standard & Poor's. They were originally Dun & Brad. T 775-15 to 778-21.

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[779] Q. Did you ever see S-29? A. Yes, it looks similar to one that's in our files.

Excerpts from Testimony of Gordon Fowler

Mr. Laulicht: May I offer it now, [780] your Honor.

The Court: All right. • • • S-29 in evidence. T779-23 to 780-6.

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[782] Q. Now, at the time you decided to buy $1 million worth of Port Authority bonds in 1972 were you aware of the summary statement as it is so-called at the bottom of the first page of S-29? A. To the extent we had this report in our file, I suppose you could say that. Again, I don't remember specifically having read this prior to making that purchase.

Q. In February 1972 did you have any idea people were trying to push the Port Authority into mass transit. A. Yes.

[783] Q. And that is when you bought the bonds after having that knowledge. A. We had knowledge that there was activity in that direction, yes. T 782-14 to 783-4.

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[784] The Court: Did you know prior to the time that you made the purchase of $1 million in 1972, that the State of New York had adopted legislation containing a total repeal of the covenant which would not become effective until New Jersey had adopted similar legislation?

The Witness: At the time of purchase? I am quite confident at that time I was aware of this. I was aware of the action on the part of the New York State Legislature and Governor Rockefeller's trying to get it passed. Whether or not it was before or after the purchase, or when the purchase took place; let me put it this way: I am not exactly sure. I don't have that information with me.

Excerpts from Testimony of Gordon Fowler

Q. [By Mr. Laulicht] At any rate, if you did buy the bonds before that total repeal by New York in 1972, I take it from S-26 you did not go out and sell $1 million worth of bonds or whatever you were holding at that time. A. That is correct.

Q. Can you explain that to me? Why didn't you sell your bonds at that time? A. At that time I did not think it was likely that the total repeal would be adopted by both states.

Q. What did you base that opinion on? [785] A. That the Governor of New York was anxious to get this done and that the New York State Legislature would go along with him was a reasonable prospect but that the previous governor of the State of New Jersey I did not think or possibly the Legislature would act or would not necessarily go along with this.

Q. Did you have any information between June of 1972 when the New York repeal was passed and November 1972 when the bi-state governors' agreement was announced with respect to what the position of New Jersey would be on the total repeal? A. I can't say at the time; the period is too short.

Q. Were you aware, Mr. Fowler, in 1972 that there was litigation relating to the covenant upon which you say you relied? A. Are you referring to litigation brought by Mr. Kheel?

Q. Yes. A. Or the firm that he was associated with?

Q. Yes. Were you aware of it at that time? A. I was aware that there was such litigation. The exact timing I can't say for certain.

Mr. Laulicht: I would like to mark S-30, the document that had been originally marked P-106.

Excerpts from Testimony of Gordon Fowler

Q. Do you remember whether you saw S-30, [786] Mr. Fowler? A. It looks similar to the report that we have in the file.

Q. Would you take a look at Page 9? Would you specifically refer to the next to the last paragraph about pending litigation concerning the covenant on which you say you relied? A. Beginning in early 1971?

Q. Yes. A. Yes.

Q. Does that paragraph refresh your recollection that you knew in or about February 1972 about the litigation challenging the constitutionality of the covenant upon which you say you relied in buying Port Authority bonds? A. You mean do I know that there was such a suit?

Q. No. Does it refresh your recollection at all that you probably knew about the lawsuit in February 1972? A. Probably, yes, sir.

Q. Is it likely that you bought that whole million dollar's worth of 38th series before February 1972 or the million dollar's worth of Port Authority bonds—let me withdraw the question and ask you whether it is likely that you had knowledge of the Kheel lawsuit [787] challenging the constitutionality of the covenant before you bought $1 million worth of Port Authority bonds in 1972? A. Yes. As I say, I don't know when in 1972 we bought them. But it is likely that I had a knowledge of it. T 784-1 to 787-6.

• • •

Q. Now, as I read S-26 and as I understood your testimony in 1973 Connecticut General bought $3 million worth of the 40th series of consolidated bonds; is that correct? A. That is correct.

Excerpts from Testimony of Gordon Fowler

Q. That would be after the date of issuance of those bonds which I believe was somewhere around June 20, 1973. A. I think it was on the day the bonds were marketed that we bought them directly as part of the new issue.

Q. It would have been somewhere around June 1973, I think I could represent that that is when this issue was marketed. A. Yes.

[788] Q. It is also true that in 1973 Aetna bought $2 million worth of 33rd series. A. That is correct.

Q. This was done at the time you were aware of the Kheel lawsuit, is that correct? A. Yes.

Q. Were you also aware that a gentleman named Brendan Byrne was running for governor in 1973? A. Yes.

Q. Were you aware prior to June 1973 when you bought $3 million of 40th series that Mr. Byrne who was then running for governor had issued a press release in which he said: We must reopen the fight to pledge surplus Port Authority revenues to essential transit projects, something Governor Cahill has refused to do. T 787-12 to 788-16.

• • •

[789] A. I became aware of Governor Byrne's position, but whether it was at that time or later time—I was aware of it after his election to office, I'm sure of that, but not necessarily prior to that point in time. I did not follow his campaign that closely.

Q. Were you aware in 1973 of Governor Rockefeller's position with respect to the repeal of the covenant? A. Yes, I was.

Q. What was Governor Rockefeller's position? A. He was anxious to have it repealed.

Q. How soon after Governor Byrne was elected and was now governor did you become aware of his position on the repeal? • • •

Excerpts from Testimony of Gordon Fowler

A. It was sometime prior to our sale of 40th series bonds, because it became evident that New York State was in favor of repeal, and that now with the new governor it was more likely that the New Jersey Legislature and the governor would go along with it.

Q. When did you make that sale of the consolidated bonds in 1974? A. In March.

Q. At that time did you try to dispose of [790] your other holdings? A. No. I just tried to get rid of the three million of the 40th series.

Q. Even though you thought that they were protected by the covenant as you testified? A. That is right.

Q. Can you explain that? A. Well, obviously they are not protected directly. They are only protected indirectly.

Q. And so? A. And so I was concerned based on the actions taken by the two legislatures that it might be possible to devise some sort of means to shelter the bonds that were subject to the covenant to the detriment of those that were not.

[791] Q. Were you concerned that something might be done to the covenant itself in early 1974? A. Yes, I was concerned, but the two legislatures and the governors would be successful in having it repealed.

Mr. Laulicht: We will mark as S-31 a document that had been previously marked P-112 and is a Moody's Credit Report dated June 14, 1973.

Q. Mr. Fowler, do you recall reading S-31 before you bought the $3 million worth of consolidated bonds of the Port Authority discussed in this report? A. I most likely did.

Excerpts from Testimony of Gordon Fowler

Q. Do you think it is likely you would have invested $3 million of Connecticut General's money without reading a report like this? A. I would have read the official statement. And I would prefer to put emphasis on that rather than on these credit reports.

Q. Were you aware when you put down $3 million that there was a discussion of the Port Authority putting up between $250 and $300 million of its own money on railroad mass transportation projects? A. I was aware that there were projects being discussed that would cost that much, yes.

[792] Q. Do you recall if some of the discussion at that time was to the effect that this would be done on a self-supporting basis? A. Yes.

Q. Do you recall that the reason for saying that it would be done on a self-supporting basis would be so that it would comply with the covenant? A. I believe that was correct.

Q. And in fact if the projects involving 250 or $300 million worth of Port Authority money was certified as self-supporting over the next ten years it would comply with the covenant, would it not? A. I believe it would.

Q. Before you bought $3 million worth of 40th series bonds that were indirectly protected, as you say, by the covenant, didn't you think that there was any way in which a Port Authority investment of $250 million in rail transportation projects could be made self-supporting? A. Did I think that there was any way that it could be made self-supporting?

Q. Yes. A. With a subsidy.

Q. What kind of subsidy? A. From the State of New York or New Jersey.

[793] Q. And that is what you thought would happen? A. I thought that there would be a combination of federal, state and local subsidies in one form or another.

Excerpts from Testimony of Gordon Fowler

Q. That is correct. That was part of the $650 million program, is that right, that was discussed at that time? Do you remember that? A. I do not remember that specific number.

Q. Do you have any idea of the debt service on $250 million worth of Port Authority bonds? A. Assuming 30-year bonds?

Q. Yes. What is the annual debt service? A. About an 8 percent constant at that point.

Q. So that it would be roughly 20 to $25 million a year? A. Yes.

Q. And you thought that is what the state and federal government would subsidize? A. If they wanted the Port Authority to get involved in it.

Q. Were you concerned that there might be a way or that there might be an effort to find a way to avoid that kind of commitment? A. Well, the fact that people were trying to repeal the covenant was indicative of the fact that there was something, either that project or some other projects [794] might be in the winds.

Q. And yet you went ahead and bought $3 million of the bonds discussed in S-31. A. Certainly. The covenant protected us.

Q. What does the covenant protect you from, Mr. Fowler? A. It protects us from the Port Authority incurring additional rail passenger transit deficits.

Q. Unless they are certified. A. They can't certify a deficit, to my knowledge.

Q. Yes, but it is possible to certify an operation as self-supporting, is it not, even though it may run a deficit? Or do you feel that there was no way that that would happen?

Excerpts from Testimony of Gordon Fowler

A. Do you mean that the Authority would in this manner certify something as being operated on a profitable or self-sustaining basis, not that it would be operated at a deficit?

Q. That is correct. A. We have to put some reliance—we put a good deal of reliance on the good faith.

Q. Of the Port Authority? A. Of the Port Authority.

Q. That is one of the reasons why you now have $7½ million worth of their bonds, that you have [795] some faith and reliance in the Port Authority. A. In being honest people, yes. T 789-1 to 795-2.

• • •

[799] Q. You say you attempted to sell more of the 40th issue but were unable to do so? A. We sold two million out of our three million and we tried to sell the remaining million.

Q. You were unable to do so? A. We were unable to do so without taking a loss.

Q. What price did you sell the two million you did sell at? A. Par.

Q. When was that ? A. In March of 1974.

Q. Tell us what particular provision in the covenant you relied on? A. Well, my general understanding of the covenant is, what is in the official statement, and part of it that is most important to me is that the mass rail [800] deficit is limited as to future projects. T 799-10 to 800-1.

Excerpts from Testimony of Gordon Fowler

• • •

Q. Are you familiar with the Consolidated Bond Resolution of October 9, 1962 of the Port Authority? A. I have read it and have an understanding of sorts of it, yes, sir.

Q How about the series resolutions [801] establishing particular issues of Port Authority Bonds? Are you familiar with those resolutions? A. Not all of them, no.

Q. Are you familiar with those of the 40th series?

A. Yes, I have read it. T 800-21 to 801-5.

• • •

Excerpts from Transcript of Hearing, February 11, 1975

[823] Mr. Sovern: Yes. I am reading from the New York Times dated February 11, 1975, which reports the bid and asked prices of the two bonds as they were yesterday.

The Port 6 was bid 87 and the Mass Port 6 was bid 89. T 823-7 to 823-12.

• • •

[840] Mr. Sovern: We turn now to the [841] Armstrong deposition transcript, your Honor. And we propose to offer a few limited extracts from the transcripts along with some exhibits.

It is our purpose, first, to offer from Volume I—

Mr. Landis: Your Honor, if I may interrupt at this point, I think I may save a lot of time, because I think under the rule that we are entitled to have the entire deposition marked in if they propose to offer excerpts from it. Then I would—

The Court: Oh, no, that is not the rule. That is not what the rule is.

Mr. Landis: I read any party may offer any other parts in the rule.

The Court: Yes, such as—

Mr. Landis: Rule 4:16-1(d).

Mr. Sovern: I am sure your Honor knows that that is not the practice under that rule with respect to the deposition of a witness.

Mr. Landis: Well, the only case that we were able to find indicates that it is the practice.

[842] The Court: Rule 4:15?

Mr. Landis: 4:16-1, your Honor, and it is part (d). It is the last phrase that I am talking about.

The Court: Well, you don't get to offer the whole deposition.

Excerpts from Transcript of Hearing, February 11, 1975

Mr. Landis: I believe any other parts means the whole.

The Court: No, you introduce any other part which ought, in fairness, to be considered with the part introduced.

Mr. Landis: I am not talking about that phrase, your Honor. I am talking about the last phrase, your Honor, I am talking about the last phrase, any part in the offer.

Mr. Sovern: That is intended to be modified by the passage that the Judge just read.

Mr. Meyner: It is not.

Mr. Landis: I don't think so at all. I have a case that I can read—

The Court: Well, I am telling you that this been the practice, that a party offering his adversary his party's deposition [843] is not subject to having the whole of the deposition introduced, only so much as is necessary to make it fair and make sense or the meaning in which the portion is introduced clear. T 840-25 to 843-6.

• • •

[850] Mr. Sovern: I would like next, your Honor, to read into the record a paragraph from a letter of January 24, 1975, from Mark K. Sisitsky to Murray Laulicht. I am reading from paragraph 6 at page 2 of that letter.

The Trust Company holds in discretionary account $2,570,000 par value of series 40 and $385,000 par value of series 41. T 850-13 to 850-21.

Letterhead of

SUPERIOR COURT OF NEW JERSEY

CHANCERY DIVISION

[SEAL]

GEORGE B. GELMAN
JUDGE

COURT HOUSE
HACKENSACK, NEW JERSEY 07601

March 10, 1975

Robert Meyner, Esq.
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Re: United States Trust Company v.
State of New Jersey—Docket No.
L-26861-73

Gentlemen:

I have read all of the communications with respect to defendant's offer of the Armstrong deposition and exhibits, and plaintiff's counter offer of excerpts from the Armstrong deposition and exhibit, as well as the proposed orders that were submitted by each side. I have also read the cases which have been cited by both sides. Finally, I have also read all of the proffered excerpts from the Armstrong

deposition and have reviewed the exhibits which both sides wish to offer.

I have come to the conclusion that the defendant should be permitted to withdraw its offer of excerpts from the Armstrong deposition and the exhibits associated therewith, and counsel for the defendant may submit an order to that effect.

Having read the materials I am satisfied that neither the offer made by the defendants or that of the plaintiff adds anything of significance to the record in this case. Further, much of the material which the plaintiff wishes to offer will be subject to objections based upon the rules of evidence.

I will ask Mr. Laulicht to submit an order under the five-day rule.

Yours very truly,

GEORGE B. GELMAN
George B. Gelman, J.S.C.

GBG:jm
cc: Dean Michael I. Sovern
Carter, Ledyard & Milburn, Esqs.

Addition to Appendix by Stipulation

[The following was added to the Appendix by Stipulation Among Counsel dated August 4, 1976]

On July 8, 1976 the Port Authority issued and sold $100 million principal amount Consolidated Bonds Forty-second Series, due 2011 (first installment). This was the Port Authority's first long-term financing since the 1974 repeal of the 1962 Covenant. The interest rate on the issue was 8.20%; the underwriting syndicate which purchased and resold the issue bid 98 ($980 per $1,000 principal amount), resulting in a net interest cost to the Port Authority of 8.27%. The issue was rated "A" by both Moody's and Standard & Poor's.

On Friday, July 9, 1976 *The Wall Street Journal* contained the following report with respect to the issue:

> About $166 million of new tax-exempt revenue bonds were marketed by two agencies, including $100 million by the *Port Authority of New York and New Jersey* and about $66 million by the *Rhode Island Housing and Mortgage Finance Corp.* The Port Authority's bonds were entirely sold and just $4 million remained available from the Rhode Island unit's issue, which was priced to yield between 4.5% in 1977 and 6.6% in 1988.
>
> An 8.2% tax-free return was provided by the Port Authority's new 35-year bonds, the same as a taxable gain of almost 15% for single persons earning about $26,000 or families making about $36,000. The single-A-rated securities were sold primarily to individuals and small institutions.
>
> "Large buyers have refused to touch the authority's bonds ever since the New York and New Jersey legislatures several years ago repealed the 1962 covenant and thereby weakened the protection afforded to bondholders,' a dealer remarked. 'Also, of course, any issue from New York has been extremely difficult to sell because of the well-publicized fiscal problems here," he added.

Addition to Appendix by Stipulation

According to a tombstone announcement in the July 12, 1976 issue of *The New York Times,* the 42nd series was offered through a syndicate headed by Bache Halsey Stuart Inc. Among the investment firms listed as participating in the syndication and offering were: Dillon, Read Municipals; Kidder, Peabody & Co.; Hornblower & Weeks-Hemphill, Noyes; Loeb, Rhoades & Co.; Blyth Eastman Dillon & Co.; Shearson Hayden Stone Inc.; E. F. Hutton & Company Inc.; L. F. Rothschild & Co.; Salomon Brothers; Merrill, Lynch, Pierce, Fenner & Smith; The First Boston Corporation; White, Weld & Co.; and Weeden & Co. The announcement referred to the interest rate, the A rating by Moody's and Standard & Poor's and the offering price of par and accrued interest.

The New York Times reported as follows on July 13, 1976:

> Prices also showed gains in the tax-exempt sector. At one point yesterday the new 8.2 percent revenue bonds marketed last week at par by the Port Authority of New York and New Jersey were being quoted at 101⅛ bid and 101⅜ asked.

Standard & Poor's "Fixed Income Investor" did not contain a full report with respect to the Forty-second Series. It continued the Port Authority's A rating and reported:

> "Municipal Prices Improve
>
> "The municipal market last week continued to follow the tone set in recent weeks, quiet and firm. The $100 million Port Authority of New York and New Jersey bonds highlighted the week's new issue activity. Coming to the market for the first time since 1973, the issue attracted considerable investor interest. There was little follow-through activity in open accounts. Prices showed modest advances in the secondary market although trading was light."

Addition to Appendix by Stipulation

Moody's Investors Service, Inc. issued a municipal credit report dated July 2, 1976 regarding the Forty-second Series which said in part:

> "Port Authority of New York and New Jersey, July 2, 1976 RC, Rating: Consolidated Bonds and Notes: A Offering: $100,000,000 Consolidated Bonds, Forty-second Series, for sale on 7-8-76, Dated: 7-15-76, Due: 7-15-2001, Call: beginning 7-15-86, L.O.: Patrick J. Falvey, Authority General Counsel; Hawkins, Delafield & Wood, New York City. *Type enterprise:* bi-state agency of New York and New Jersey which operates air terminals, toll bridges and tunnels, marine facilities, World Trade Center, PATH rail transit system, other facilities including bus stations, truck terminals, heliports. *Pledged revenues:* direct and general obligations of the Authority secured equally and ratably with all other Consolidated Bonds and Notes by a pledge of the net revenues of the existing facilities of the Authority, the General Reserve Fund of the Authority, and the Consolidated Bond Reserve Fund of the Authority. *Purpose:* capital expenditures in connection with Authority bridges and tunnels; docks and wharves; airport terminal and service buildings, roadways, runways, taxiways and fuel and utility service and distribution systems; bus terminals, the Hudson Tubes portion of the PATH system; parking facilities; storage or training facilities directly related to any of these; and the World Trade Center; and for refunding all or any part of $50,000,000 Consolidated Notes, Series BB, issued in 1975; provided, that no more than 10% of the amount of the proceeds not expended to refund any Series BB Consolidated Notes shall be used for the purpose of capital expenditures in connection with the World Trade Center and those integral portions of an extension to the Port Authority Bus Terminal related to any further construction above the extension. • • •

Addition to Appendix by Stipulation

The New Jersey Supreme Court in a February 1976 decision upheld the Superior Court in the May 1975 decision that upheld the New Jersey legislation that repealed the 1962 covenant restricting Authority involvement in deficit mass transit operations. This 1976 decision has been appealed to the United States Supreme Court which recently announced that it will hear this case at its next term. These court decisions are a matter of deep concern to bondholders generally. The effect on the Authority cannot be determined at this time in the absence of a definite plan for financing mass transit projects and facilities deemed to be non-selfsupporting. In the meantime, earnings of the present facilities are good, and reserves for debt service continue strong. • • •

Expansion Program: (1) in August 1975, the Authority authorized a major rehabilitation program of the upper level roadway of the George Washington Bridge and improvements to the New York and New Jersey approach highways at an estimated $37,000,000 construction cost; (2) Bus Terminal is being extended in an area north of the present Terminal, Lincoln Tunnel approaches are being extended, and air rights above the extension would be used as an office building built and operated by private parties. Extension and Tunnel approaches including land costs, but not air rights development, are expected to involve a capital investment of $160,000,000; (3) planned rehabilitation of PATH including modernization and development of Journal Square terminal area, is estimated to require further Authority investment of about $59,000,000; (4) under construction and scheduled for completion by the end of 1976 is a multi-level parking area at La Guardia Airport at estimated $41,751,000 expenditure (5) Authority capital expenditures for a new interchange and roadway system linking the New Jersey Turnpike directly with Newark International Air-

Addition to Appendix by Stipulation

port and Elizabeth-Newark Marine Terminal would be 50% of the estimated $50,000,000 cost, with the State and Turnpike Authority funding the balance; (6) $19,000,000 is estimated as cost to build distribution buildings and pave open areas on 95 acres of undeveloped land adjoining Port Newark; (7) $12,000,000 budgeted for 1976 for continued development of Jersey Central property at Elizabeth Marine Terminal and construction of specialized container facilities; (8) present estimated are that an additional investment of $120,000,000 will be needed to complete the World Trade Center. • • •

The legislatures in the 1971-74 period enacted laws providing for the regional development of mass transportation access to Kennedy International and Newark International. The legislation also authorizes the Authority to undertake as Hudson Tubes extensions passenger rail facilities extending from Penn Station in Newark over rail transit lines to Plainfield including a connection to provide improved access to Newark International. In October 1974 a joint task force of the New Jersey Department of Transportation and the Authority was established at the request of Urban Mass Transportation Administration (UMTA) of the U.S. Department of Transportation to study potential transit alternatives in the Newark-Plainfield corridor. The task force submitted its interim report on 1-15-75 to Governor Byrne, and the report assessed in detail recommendation 5 transit alternatives in the Union County corridor as well as transit access to Newark International. A final report was submitted to UMTA on 2-10-75.

The 1971-74 legislation also authorizes the Authority to undertake certain improvements to passenger rail line connecting with the Hudson Tubes to provide direct rail service into Penn Station in New York City by the Erie-Lackawanna and to upgrade

existing Penn Central rail service into Penn Station in New York City. The legislation adopted in 1974 also provided for the repeal of the statutory covenant between the two states and affected bondholders limiting the Authority's ability to participate in deficit passenger rail projects.

The Authority in May 1975 filed an application with UMTA for $277,600,000 to pay part of the cost of extending PATH to Plainfield. Local contribution totals $69,400,000 to be funded by the Authority from proceeds of future bond issues. It is contemplated that PATH would enter into an agreement with New Jersey under which PATH would acquire the properties out of Authority bond issues and UMTA grants and lease the property to the State. The amount of rent to be paid by the State would depend mainly on the outcome of the litigation relating to repeal of the statutory covenant. On 12-19-75, UMTA rejected the application as filed for Federal aid, and this decision is currently being considered by UMTA.

After consultation with both Governors, the Authority Chairman has noted that the revision of Authority bridge and tunnel tolls effective 5-5-75 is expected to result in additional revenues to the Port Authority of more than $40,000,000 per year and that these additional revenues could support $400,000,000 in capital improvements in mass transportation projects authorized for Authority participation: $160,000,000 allocated to the extension of the Bus Terminal now under construction, and the remaining $240,000,000 for authorized mass transit projects in each state in accordance with priorities established by responsible State officials and the Authority commissioners acting pursuant to legislative authorization and commitments to holders of Authority obligations.

In recognition of the loss of manufacturing jobs and plants in the Port District over the last two decades, in February 1976 the Authority authorized

the initiation of discussions with appropriate officials in both states and undertaking of a major study of industrial development needs in the Port District, including an investigation of energy availability and costs.

Toll Rates: Bridge and tunnel tolls were revised 5-5-75 including a 50% increase in auto tolls and 100% increase in the cost of a 30-day commutation ticket; it is estimated that the higher tolls will result in $40,000,000 additional revenues annually, with the increased toll revenues expected to enhance the Authority's ability to undertake additional mass transit projects. On 4-25-75, after receiving complaints, the Federal Highway Administrator began an investigation which will include a public hearing to determine whether the toll increases are just and reasonable. On 5-6-75, the Administrator served on the Authority a copy of a motion filed with the Administrator by a complainant for an order requiring the Authority during the pendency of the toll proceedings to create an escrow account for receipt of the revenue from the toll increase. On 5-23-75, the Authority filed a memorandum opposing this motion, and the decision on this motion is still pending. The FHA issued a notice of proposed rule making on 7-18-75 to govern bridge toll receipt procedures which would require a 90-day advance notice of a proposed toll increase and would also require the escrow of all toll increase revenues on commencement of any proceeding to determine if the increase is just and reasonable.

Litigation: On 4-30-74, United States Trust Company of New York commenced an action in New Jersey Superior Court, Bergen County, on its own behalf, as Trustee for the 40th and 41st series of Consolidated Bonds and on behalf of holders of all Consolidated Bonds, against New Jersey and the Governor and Attorney General of New Jersey, seeking a declaratory judgment that the action taken in

Addition to Appendix by Stipulation

1974 to repeal the 1962 statutory covenant that restricted the Authority involvement in deficit mass transit operations violates both the United States and New Jersey Constitutions. The plaintiff alleged in its complaint that as a result of the covenant repeal, the secondary market for Consolidated Bonds has been and will continue to be adversely affected to the deteriment of all holders. The defendants' answer denied this allegation. On 5-14-75, the validity of the 1974 action repealing the 1962 statutory covenant was upheld by the Superior Court, and this decision was affirmed on 2-25-76 by the New Jersey Supreme Court. On 5-14-76, the U.S. Trust appealed this decision to the United States Supreme Court, and on 6-28-76 the U.S. Supreme Court agreed to hear this matter during its next term.

On 5-20-76, another appeal to the U.S. Supreme Court was taken in a companion New Jersey case, instituted by a New Jersey resident who had sought unsuccessfully a judicial declaration that the 1962 statutory covenant was invalid.

On 6-17-74, U.S. Trust Company instituted an action in New York in the Supreme Court, New York County, against New York State and its Governor and Attorney General, which is still pending. This action is similar to the Trust Company's New Jersey action except that a declaration is sought that the statutory repeal violates the New York Constitution rather than New Jersey's Constitution."

On July 7, 1976, the day before the issue and sale of the Forty-second Series, outstanding Port Authority 6% Bonds were quoted at 81 bid and outstanding Port Authority 5½% Bonds were quoted at 73 bid.

The following bid prices were reported by *The New York Times* on July 9, July 13 and August 4, 1976:

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		Due	July 9 Bid	July 13 Bid	August 4 Bid
Indiana Toll Road	3½%	1/1/94	81½	82	83½
Kansas Turnpike	3⅜%	10/1/94	82	82	84
Mass Port	3.80%	2004	62	63	63
Mass Port	6%	2011	85	85	85
Port of N. Y.	4¾%	2003	64	64½	64½
Port of N. Y.	5½%	2008	72	72	73
Port of N. Y.	6%	2008	80½	81	82½

Addition to Appendix by Stipulation

[Letterhead of]
DEPARTMENT OF TRANSPORTATION
URBAN MASS TRANSPORTATION ADMINISTRATION
WASHINGTON, D.C. 20590

SEAL OF
THE ADMINISTRATOR

March 9, 1976

Mr. Alan Sagner
Commissioner
State of New Jersey
Department of Transportation
1035 Parkway Avenue
Trenton, New Jersey 08625

Dear Commissioner Sagner:

Since my December 19, 1975 decision on the PATH extension I have received numerous inquiries from members of the New Jersey Congressional delegation and from others regarding the status of that and other transit projects in the State. Press reports in early February stimulated several such questions. I am writing this letter to summarize the situation from UMTA's point of view, and am taking the liberty of sharing it with those who have sought information on these matters.

The December letter said that UMTA would be willing to consider a multi-year capital funding commitment to a package of transit improvement projects which the State might develop based upon a comprehensive transit plan and multi-source capital program. I indicated that $300-350 million might be available through Fiscal Year 1980 to support such a program under certain conditions. I further indicated that as an alternative we would be prepared to go

Addition to Appendix by Stipulation

forward on the traditional basis of single project applications for the Erie Lackawanna and New York and Long Branch improvements if you preferred, but that we would entertain a resubmission of the PATH project only as part of a comprehensive package and only at a much reduced cost to UMTA's discretionary capital grant budget. We have since made a $39 million grant for railcar purchases on the Erie Lackawanna line on this basis.

In meetings and conversations since December, you have indicated that the State would be interested in pursuing the comprehensive plan and package approach, and I know that you are working actively to develop such a submission. You have raised the question of whether the UMTA support for such a package might be raised to $400 million, and we are reviewing that question. I have indicated to you that any Federal commitment in the $300-plus million range would consume the full allocation of Section 3 capital grant funds which we could make to the State through Fiscal Year 1980 under current authorizations.

I would recite here the specific elements which my December letter and our subsequent discussions indicated should be forthcoming if you wish to follow the package approach:

1. You should submit a comprehensive transit plan and all-source capital program for the State, covering the period through Fiscal Year 1980;

2. That plan should include any necessary updating of your commuter rail program to reflect the enactment of the Railroad Revitalization and Regulatory Reform Act of 1976, and should consider the establishment of an authority to operate commuter rail service within New Jersey or on a bi-State or tri-State basis. The plan should also include attention to bus service, given the importance of that form of transit in serving passengers in your State;

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3. The December letter said that the transit plan "should be consistent with a comprehensive land use plan for northern New Jersey." As you know, this is a requirement of the UMTA legislation; it is not meant to stimulate the development of any new land use plan, but only to observe the legal requirement that transit programs be consistent with comprehensive land use plans; and

4. The comprehensive transit plan and capital program are to be developed by the State "together with appropriate regional planning bodies," which in this case would mean the Tri-State Regional Planning Commission since your funding applications to UMTA will apparently be confined to northern New Jersey projects. This again has reference to UMTA's statutory requirements, but I think the regional planning process takes on special significance where multi-year proposals are being submitted which would preempt all UMTA funding for the State through Fiscal Year 1980 under our current authorizations. I am sure that both we and you want to be sure that there has been adequate public discussion of such important priority setting and resource allocation steps.

If you do decide to resubmit the PATH project in a way that is responsive to the above conditions, we would want to be sure that your submission clarifies two issues which have been raised throughout the history of our review of your earlier applications:

1. You should indicate what service you intend to provide west of Plainfield; and

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2. You should include in the comprehensive plan and capital program the necessary feeder bus and automobile parking facilities needed to support ridership on the rapid transit system. Some source of capital funding for these ancillary services should be specifically indicated and committed to, along with the funds needed to match the Federal contribution for the PATH extension itself.

Finally, we ask you to seek to conclude an agreement with building contractors and construction unions whereby any labor disputes which might occur during the course of PATH construction could be settled without costly work stoppages. This follows a national policy which Secretary Coleman is seeking to implement in connection with all major construction projects financed by the Department of Transportation.

I hope that this letter clarifies any questions which you or others may have regarding the status of these projects. We look forward to continuing to work with you in improving public transportation service in New Jersey.

Sincerely,

ROBERT E. PATRICELLI
Robert E. Patricelli

Addition to Appendix by Stipulation

[Letterhead of]
STATE OF NEW JERSEY
DEPARTMENT OF TRANSPORTATION

ALAN SAGNER
Commissioner

May 11, 1976

Dear Mr. Patricelli:

I am writing in response to your letter of March 9, 1976 in which you summarized, from UMTA's point of view, the status of the PATH Extension and other transit projects in our State.

In order to be as responsive as possible I shall respond to your letter question by question although some of the answers are clearly related.

I trust that your questions are resolved and that we shall receive prompt approval of this program. The people of our State have been waiting much too long for these critical projects.

Sincerely,
ALAN SAGNER
Alan Sagner
Commissioner of Transportation

MR. ROBERT E. PATRICELLI
Administrator
Urban Mass Transportation Administration
Department of Transportation
400 7th Street, S.W.
Washington, D.C. 20590

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Page 2
Question 1

"You should submit a comprehensive transit plan and all-source capital program for the State, covering the period through Fiscal Year 1980;"

New Jersey was one of the first states in the country to recognize the need for a comprehensive approach to transportation when it created the Department of Transportation in 1966, to replace the Department of Highways. In doing so it recognized the need for coordination of all modes of transportation and importance of adequate public transportation to meet the needs of the changing social and economic environment. The State of New Jersey was the first state to take an active role in the preservation and improvement of public transportation with the payment of a rail passenger subsidy in 1960. This program of subsidy has grown over the years until there were four railroads and numerous motorbus carriers receiving payments to cover operating deficits. To date the state has paid out over $200 million in operating expenses to continue essential services.

To give further structure and guidance for action the department has prepared, in 1968, and 1972, two master plans and is now in the process of preparing a third. These plans as well as various other documents, including the Transit Development Program, have consistently identified as state priorities the preservation and improvement of essential rail service in existing corridors and the supplementing and complementing of that service by bus service.

In addition a number of landmark studies have been performed during this period and the information gained from these studies has been invaluable in assisting the shaping of a coordinated public transportation system. A

number of technical feasibility studies are now underway or are soon to be underway and each of these studies will provide the basis for informed decisions on matters of future capital improvements, and, just as important, operational changes intended to provide the highest level of public transportation service at the most economical cost. • • •

The most recent document describing our comprehensive state transit plan is the 1972 Master Plan as supplemented by the *New Jersey Transit Development Program, 1974-1979.* In the 1972 Master Plan three critical rail corridors were discussed as being of high priority: • • • the Union-Somerset Corridor, • • •

The Erie Lackawanna: Morris and Essex Division, • • •

[and] the Coastal Section [, listing] the New York and Long Branch improvements. • • •

The *Master Plan '72* was followed by the development of the *New Jersey Transit Development Program, 1974-1979.* This document was submitted to Administrator Herringer in September, 1973, and represents the first statewide public transportation capital improvement program prepared in the United States. This document was prepared according to the standards established by the *Urban Mass Transportation Planning Requirements Guide* to meet the requirements of the Urban Mass Transportation Act of 1964 and its later amendments. Within this document, the reelectrification of the Morris and Essex Division of Erie Lackawanna, the electrification of the New York and Long Branch, and the extension of PATH to Plainfield are all discussed. • • •

On the assumption that New Jersey would be entitled to only $400 million through Fiscal Year 1980 from existing UMTA authorizations we would undertake the following high priority projects:

—PATH extension to Plainfield including equipment.

—Reelectrification of the Morris and Essex Branch of the Erie Lackawanna including electrification from Dover to Netcong and purchase of MU equipment.

—Electrification of New York & Long Branch from South Amboy to the vicinity of Red Bank including purchase of MU equipment.

Table I contains the financial information for the above three projects and calls for additional UMTA funds of $482 million. This exceeds the expected allocation of $400 million, however, by $121 million. ($82 million plus $39 million recently granted for the Erie Lackawanna project.)

The Department of Transportation will fund the balance of $121 million as follows:

—increase local share for PATH project of $50 million to be provided by the Port Authority of New York and New Jersey.

—transfer of highway funds, both Interstate and Federal Aid Urban Systems (FAUS) in an amount of $71 million.

TABLE I

PUBLIC TRANSPORTATION PRIORITY CAPITAL PROGRAM

	Total	UMTA	Local	UMTA to Date	UMTA Balance
PATH	347	278	69	0	278
EL	265	212	53	118	94
NY&LB	137	110	27	0	110
	749	600	149	118	482

• • •

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QUESTION #3

> The December letter said that the transit plan "should be consistent with a comprehensive land use plan for northern New Jersey." As you know, this is a requirement of the UMTA legislation; it is *not meant to stimulate the development of any new land use plan, but only to observe the legal requirement that transit programs be consistent with comprehensive land use plans; and*

"The transit plan of the State of New Jersey is consistent with the comprehensive land use plan for Northern New Jersey. The transit plan for New Jersey has been developed in conjunction with the Tri-State Regional Planning Commission, the designated comprehensive planning organization for the region."

• • •

As you know all three of these priority projects have been endorsed by the official metropolitan Planning Organization, as well as by the unofficial but highly respected Regional Planning Association, as being consistent with the transportation needs of the region as they relate to the overall economic development and land use objectives. In the case of the NY & LB and the EL, this was recognized by UMTA prior to their granting of a "letter of no prejudice" in the case of the former and an actual grant in the case of the latter.

With regard to PATH allow us to restate the positive steps New Jersey has taken, will be taking, and is prepared to do, particularly as they relate to the relationship of the PATH extension and land use plan in the PATH service area.

The affected communities along the Path corridor have endorsed the project, and have committed themselves to

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utilize their authority to support the PATH project's non-transportation objectives. We call your attention to the April 1, 1974 submission, appendices B & C. As previously pointed out to you, Union County has already set in motion the organization for resolving various development issues arising from the PATH extension project. This is the Union County Transportation Advisory Committee, which will function in concern with a Station Areas Needs Study. Parking, traffic management, land development, and environmental improvement will be under review. The citizen input through the Advisory Committee will focus on local problems. This Department supports this activity and has representation at meetings and discussions.

The City of Newark, in anticipation of PATH, has proposed several major development projects. This includes a sports and entertainment coliseum in downtown Newark adjacent to Pennysylvania Station and a $15 million hotel/commercial complex adjacent to the proposed McClellan Street PATH station, creating 500 new jobs. PATH would also further ongoing Newark revitalization projects and improve accessibility for Newark Airport. Inadequate ground access to the airport is repeatedly identified as an impediment to airport usage.

In addition, PATH will help in the redevelopment and revitalization for the urban areas along the corridor, and provide needed service for both the blue collar and white collar residents of both urban and suburban communities, consistent with local planning efforts as well as statewide plans.

The Port Authority of New York and New Jersey has played a major role in the over-all revitalization of the region. In addition to earmarking additional automobile tolls for public transportation uses, including PATH, the Port Authority is actively studying potential industrial

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development sites within the port district, most of which involve cities served by PATH, further adding to the value of a PATH extension as a critical transit spine for a growing economic development function.

The State of New Jersey recognizes the responsibility incumbent upon the state in providing for the efficient allocation of land resources. Governor Byrne, in his Annual Message delivered on January 13, of this year, declared:

> I strongly support the concept of local control of zoning but the inevitable regional impact of large-scale projects must be taken into account. The Development Review Act I have proposed will provide such an overview in accordance with state guidelines. Such an approach is essential to rational, coordinated land use and planning.
> Under this act, the State will identify areas suitable for major economic and residential development and also designate areas that require special protection from such development. Thus, major capital investment decisions can be coordinated with broad land-management policics. Both are vital if we are to arrest the urban sprawl that has disfigured much of New Jersey and so damaged our economy and environment.

Furthermore endorsing the PATH proposal, Commissioner Sheehan of the Department of Community Affairs, referred to this proposal, stating that "two things appear certain to be incorporated into the comprehensive development plan. First, there will be a commitment to the revitalization of our older urban areas; and secondly, there will be a commitment to preserve, as much as possible, New Jersey's currently undeveloped farmland and open space." (Letter attached plus letter from Commissioner Bardin of the Department of Environmental Protection).

Addition to Appendix by Stipulation

[Letterhead of]
STATE OF NEW JERSEY
DEPARTMENT OF ENVIRONMENTAL PROTECTION
DAVID J. BARDIN, COMMISSIONER

May 27, 1975

Honorable Alan Sagner
Commissioner
Department of Transportation
1035 Parkway Avenue
Trenton, New Jersey 08625

Dear Commissioner Sagner:

In response to your request, the Department of Environmental Protection has briefly reviewed the general proposal by the Port Authority of New York and New Jersey to extend PATH transit service from Newark to Plainfield, including the Environmental Report prepared on the project by the Port Authority of New York and New Jersey. On the strength of our initial review, the Department of Environmental Protection endorses the basic concept of this PATH extension and offers the observations noted below regarding air quality.

The Department of Environmental Protection endorses the concept of increasing the State's mass transit capacity in order to reduce the dependence on the private automobile, to reduce net air pollution emissions and to conserve energy. It appears to us that the PATH extension would help achieve these goals. The implementation of the PATH extension will reduce the total number of vehicular miles driven in the northeastern portion of New Jersey and thus

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be consistent with the State's "Transportation Control Plan" for achieving air quality as called for by the Clean Air Act.

Moreover, the Department's Bureau of Air Pollution Control has compared the PATH extension with various alternatives presented in the Environmental Report, including commuter service by the Central Railroad of New Jersey. Based on the review of the Environmental Report, the Bureau concurs that an electrically-operated PATH system to Plainfield would result in an overall improvement in air quality. It should be noted that the anticipated net improvement reflects: (a) reduced emissions (CO, NO_x, particulates and hydrocarbons) from many automotive sources operating in a relatively small area; (b) increased emissions (SO_x, NO_x, and particulates) from a few electric power generating stations widely dispersed over a large area; and (c) reduced emissions (NO_x, particulates and hydrocarbons) from the CNJ diesel-powered locomotives operating in a relatively small area. Reflecting all of the foregoing, the Report shows a net air quality improvement under the PATH extension.

FAITHFULLY,

DAVID J. BARDIN
David J. Bardin
Commissioner

Addition to Appendix by Stipulation

[Letterhead of]
STATE OF NEW JERSEY
DEPARTMENT OF COMMUNITY AFFAIRS

PATRICIA Q. SHEEHAN
COMMISSIONER

May 14, 1975

The Honorable Alan Sagner, Commissioner
New Jersey Department of Transportation
1035 Parkway Avenue
Trenton, New Jersey 08625

Dear Commissioner Sagner:

At your request, we have reviewed the proposed extension of the PATH line from Newark to Plainfield, on the basis of the State's overall land use needs and the State's growth and development plan. We would offer the following comments.

While New Jersey, like most other states, has delegated planning and zoning responsibilities to local units of government, it does retain the right to provide overall planning and policy guidance. This guidance is particularly appropriate for investments made by the State for the benefit of more than one municipality, and which can have lasting developmental effects. Under the legislative mandate granted to it, the Department of Community Affairs has overall responsibility for providing a growth and development plan for New Jersey.

The work of the planning staff is going forward, and by the end of the next fiscal year, a draft of the comprehensive development plan will be published. After thorough discussions with municipalities and counties, with other

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State Departments, and with land use, energy, and other resource experts, two things appear certain to be incorporated in the comprehensive development plan. First, there will be a commitment to the revitalization of our older urban areas; and secondly, there will be a commitment to preserve, as much as possible, New Jersey's currently undeveloped farmland and open space.

In light of this consensus and other considerations related to the future development of the State, it is our judgment that the PATH extension is most consistent with the evolving overall growth and development strategy. First, it would provide a needed boost to the redevelopment of Plainfield, as well as assisting the rehabilitation of other urban areas along the route of the PATH extension. Secondly, it would make the whole corridor between Plainfield and Newark more attractive for development and redevelopment and attract growth into that area. This redevelopment would replace the pattern of dispersal which is so wasteful of land and energy resources. This, we think, will help preserve other areas of the State as productive farmland or as open space. Finally, there are other important positive benefits in providing linkages between residences and work places, and in providing additional employment opportunities at a time when they are so badly needed.

For these reasons, we are happy to join with you in endorsing the PATH extension and urging its prompt approval, funding and construction.

Very truly yours,

PAT Q. SHEEHAN
Patricia Q. Sheehan

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Page 2
Question 4

> "The comprehensive transit plan and capital program are to be developed by the State "together with appropriate regional planning bodies," which in this case would mean the Tri-State Regional Planning Commission since your funding application to UMTA will apparently be confined to northern New Jersey projects. This again has reference to UMTA's statutory requirements, but I think the regional planning process takes on special significance where multi-year proposals are being submitted which would preempt all UMTA funding for the State through Fiscal Year 1980 under our current authorizations. I am sure that both we and you want to be sure that there has been adequate public discussion of such important priority setting and resource allocation steps."

The comprehensive public transportation plan we have been describing above, as well as the supporting capital program, have been developed in conjunction with both the Tri-State Regional Planning Commission and the Delaware Valley Regional Planning Commission. The most recently published public transportation Master Plan of the TSRPC, *Maintaining Mobility,* issued in September 1975, lists, as priority projects, the extension of PATH to Plainfield, the electrification of the New York and Long Branch from South Amboy to the vicinity of Red Bank and the acquisition of new passenger rolling stock for this service, the re-electrification and re-equipping of the Morris and Essex Division of Erie Lackawanna and the Regional Bus Program.

This plan has been subjected to considerable public discussion prior to adoption and such review and discussion is continuing during the process of updating.

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The MPO (Tri-State) agrees with the Department of Transportation that the priority capital program described in question one above should receive the highest funding priority under the limited amount of funds to be provided by UMTA (attached is a letter from the Executive Director of Tri-State which supports this position). Furthermore, we in the State are fully cognizant of the fact that no such major decision can ever satisfy everyone. We feel that this issue has been discussed in a full and spirited manner both publicly and privately and we are prepared to take the praise or criticism associated with the decision to do this program. These projects are ready to go and we must move forward as rapidly as possible.

• • •

Page 3
QUESTION #1

"You should indicate what service you intend to provide west of Plainfield":

The Department has been deferring, with Tri-State and UMTA's knowledge, the start of the technical feasibility study of *public transportation services to be offered west of Plainfield,* pending receipt of a decision from UMTA on the proposed PATH extension. The study design for this effort has been modified to take into accounting the changing circumstances of ConRail's inception and this work program will soon be submitted for approval. Alternate public transportation services to the west of the proposed terminus of PATH will be considered, including:

- the further extension of PATH
- suburban railroad service
- light rail transit service

Addition to Appendix by Stipulation

- feeder bus service to PATH at Plainfield
- closed door commuter rail service to Newark
- existing bus service to Newark and New York

The study will encompass the territory along the CNJ to the vicinity of Phillipsburg and also the territory along the former Reading Company lines from their connection with CNJ at Bound Brook westward to the last station in New Jersey at West Trenton. This study will be performed in conjunction with the planning staffs of the counties the lines traverse and will present, upon completion, a workable public transportation system to connect with PATH at Plainfield. This service, to the west of Plainfield, can be planned, equipped, and placed in service by the time PATH service is initiated at Plainfield.